The Economist

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Politics this week

Jul 7th 2005
From The Economist print edition

London under attack

Reuters

London was rocked by a series of **explosions** on its transport network during the morning rush hour on July 7th. Initial reports said that at least six blasts had occurred at several points along the city's densely populated underground system and on a bus in the city's centre, causing deaths and injuries. Britain's prime minister, Tony Blair, blamed terrorists, whom he described as "barbaric". The incidents took place the day after the 2012 summer Olympics were awarded to London.

See article

The events in London coincided with a meeting of the leaders of the **G8** at **Gleneagles** in Scotland. The summit focused on Africa and the global environment. Leading up to the gathering, a series of events were held in several countries under the banner of "make poverty history".

See article

Meanwhile, leaders of the 53-member African Union met in **Libya**, whose leader, Muammar Qaddafi, said that African countries should no longer go begging to the West; but the other leaders all asked for more debt relief.

See article

The OECD said that **Africa's economic activity** rose last year by 5%, its best performance for eight years. But it said that only six countries in the African Union will meet the UN's millennium development goals.

For the first time, two **Iraqi** insurgent groups named a spokesman to voice their demands, implying that they might be open to negotiation with the government. Meanwhile, an extreme Islamist group, led by a Jordanian, Abu Musab al-Zarqawi, kidnapped Egypt's envoy to Iraq and said they had killed him.

See article

Hamas, the **Palestinians'** main Islamist party, said no to an offer from Fatah, the secular-minded group that runs the Palestinian Authority, to join a unity government.

Two rebel groups from **Darfur,** Sudan's battered western province, signed a "declaration of principles" with Sudan's government to open the way to peace talks next month. But similar hopeful statements have led nowhere several times before.

Hanging up her robe

Justice Sandra Day O'Connor, a swing-voter in many of the **Supreme Court's** rulings since her appointment in 1981, announced her retirement. George Bush said he would take his time nominating her replacement, but conservative and liberal pressure groups began to churn out material denouncing candidates.

See article

A judge jailed Judith Miller of the **New York Times**, after she refused to

Getty Images

testify about her sources. In the same case, where prosecutors are trying to find out who leaked the identity of a CIA agent, Matthew Cooper of **Time** magazine agreed to testify, with the agreement of his source.

See article

The **Central American Free Trade Agreement** headed for the House of Representatives after passing the Senate by a 54-45 vote last week.

The state government in **Minnesota** was partially shut down after the Democratic state Senate and Republican governor failed to reach agreement on a budget.

See article

Not so holy

In **India**, six militants attacked a disputed religious site in Ayodhya, which is claimed by both Hindus and Muslims. Indian security forces killed all six militants, but the attack could impede India's peace process with Pakistan. Meanwhile, a high court ruled that opposition leader Lal Krishna Advani could stand trial on charges of inciting a riot at the site in 1992, in which 2,000 people were killed. Mr Advani may appeal to India's Supreme Court.

The World Health Organisation's and United Nations' animal health agencies announced a $250m strategy to combat **bird flu**, which is still ravaging South-East Asia. The announcement comes after the latest outbreak of the deadly disease, in China's province of Qinghai.

One American Navy Seal was rescued, two others were found dead and the Taliban claimed to have captured a fourth in **Afghanistan**, after a four-man team went missing in an operation against insurgents in Kunar province, in the country's east.

See article

An **Indonesian** judge agreed to reopen the case of Schapelle Corby, an Australian sentenced to 20 years in jail on charges of drug smuggling, in light of new evidence. Miss Corby's arrest did significant damage to Indonesia's relationship with Australia.

Rooting out graft

Two top officials in **Brazil's** ruling Workers' Party stepped down over cash-for-votes allegations. In a bid to contain the damage, President Luiz Inácio Lula da Silva made three ministerial changes, giving two extra portfolios to a centrist ally.

See article

In **Mexico**, the formerly ruling Institutional Revolutionary Party (PRI) won an election for governor of the state of Mexico, the country's most populous state. Opponents claimed the PRI broke campaign-spending limits.

See article

Bolivia's Congress agreed constitutional amendments to allow an early general election in December, to be followed by a constituent assembly and a referendum on regional autonomy next year. The country's president resigned last month after weeks of protests led by radicals seeking the nationalisation of the country's oil and gas industry.

Curtains for Schröder?

The **German election** campaign kicked off after Gerhard Schröder deliberately lost a vote of confidence in parliament, and his Social Democratic Party published its programme. The German president or the Constitutional Court could yet intervene, but the election looks likely to be held on September 18th.

See article

Vladimir Putin, Russia's president, held a celebration of **Kaliningrad's** 750th anniversary with France's Jacques Chirac and Germany's Mr Schröder. Kaliningrad's two neighbours, the Poles and the Lithuanians were furious not to be invited.

Fights broke out in **Ukraine's** parliament as the government pushed through controversial liberalising laws meant to get the country into the World Trade Organisation by the end of the year.

EPA

Albania's general election passed off peacefully although foreign monitors said it still fell short of international standards. The winner seems likely to be the Democratic Party of Sali Berisha, who was ousted as prime minister after a huge pyramid-scheme scandal in 1997.

See article

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Business this week

Jul 7th 2005
From The Economist print edition

EU software patents

The European Parliament rejected legislation intended to provide a European Union-wide standard for **software patents**. Large businesses, such as Nokia and Siemens, had pushed for the law, arguing it would improve research and development. But advocates of open-source software said competition could suffer, as smaller businesses would face larger legal costs.

Another semiconductor-maker launched an antitrust lawsuit against a larger rival. **Broadcom**, a firm that makes chips for use in broadband technology, accuses **Qualcomm** of monopolising the CDMA technology used in mobile phones. Last week, Advanced Micro Devices brought an antitrust suit against Intel.

Microsoft agreed to pay $775m in cash (and extend $75m in credit for software) to settle an antitrust charge laid against it by IBM. IBM's case stemmed from the antitrust suit brought by the United States Justice Department against Microsoft, which was resolved in 2002.

Concerto Software, which specialises in providing systems to call centres, agreed to buy **Aspect Communications**, a maker of software for automated call centres, in a deal worth around $1 billion. The merger should provide Concerto, which is owned by two private-equity firms, with steady revenues from call centres' increasing demand for maintenance and upgrades.

Sanyo became the latest Japanese electronics manufacturer to announce a restructuring in response to tumbling prices for consumer electronics. Over the next three years the company will cut 15% of its global workforce and close some manufacturing facilities.

General Motors said sales of new cars and trucks in the United States rose by 41% in June, compared with the same month in 2004. The increase is a response to marketing that offers buyers the same discounts that GM employees receive. GM said it would extend the plan until August. Chrysler and Ford promptly announced similar schemes.

Not banking on it?

Italy's central bank defended its handling of a bid for **Banca Antonveneta** by **ABN Amro**. The Dutch bank's chief executive criticised the Bank of Italy for “stalling” takeovers of Italian banks by foreign banks—ABN Amro extended the deadline for its *euro*7.6 billion ($9 billion) offer to July 22nd. A small Italian bank has made a rival, contentious bid.

A plan to privatise Japan's postal system by 2017 narrowly passed the country's lower house of parliament. **Japan Post**, which includes giant savings and insurance units, is by some estimates the world's largest financial institution, controlling around $3 trillion in assets.

See article

Morgan Stanley released the contract details of John Mack, who was approved as chairman and chief executive by the investment bank's board last week. The returning Mr Mack can expect to earn up to $25m a year. His pay is to be based on the remuneration of the heads of other big Wall Street firms.

See article

UnitedHealth Group, America's second biggest health insurer, announced a merger with **Pacificare Health Systems**, a rival. UnitedHealth will pay $8.1 billion and will also assume $1.1 billion of debt.

The deal will increase UnitedHealth's presence in two rapidly expanding markets: California and recipients of Medicare.

Oil in troubled waters

Chevron's vice-chairman, Peter Robertson, reportedly dismissed speculation that the company would spin off **Unocal's** Asian assets if it wins a bidding war with **China National Offshore Oil Corporation** to buy the firm. Meanwhile, the Chinese government fired a broadside at American politicians and told them to “stop interfering” in the acquisition. CNOOC's chairman, Fu Chengyu, said that politicians were overreacting to an alleged Chinese threat to energy security.

Rosneft, Russia's state-run oil company, signed a $23-billion agreement with **KazMunaiGas**, Kazakhstan's state-run company, to develop production in the Caspian Sea. Kazakhstan is estimated to have one of the world's largest recoverable reserves of energy.

See article

Medef, France's main business lobby, elected Laurence Parisot as its president, the first woman to hold the job. Ms Parisot said she would start a rapprochement with the government to reform the country's rigid labour market.

Feeling down

An upward revision to America's GDP helped the **dollar.** The pound fell to an 18-month low against the greenback. The euro fell to a 14-month low, partly on comments from a board member of the European Central Bank on the “sovereignty” of nations in the euro area.

See article

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Letters

Jul 7th 2005
From The Economist print edition

The Economist, 25 St James's Street, London SW1A 1HG
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Funding Boeing and Airbus

SIR – Your report on Boeing and Airbus asserts that legislation in Washington state gives "Boeing a tax break of $3.2 billion over 20 years" ("Nose to nose", June 25th). I served as Washington's attorney-general when this legislation was enacted. My office reviewed the legislation prior to passage and I can assure you that your characterisation of it is wrong. The state is not providing $3.2 billion in tax breaks to Boeing. This figure refers to the total estimated tax adjustment over 20 years for the 500-1,000 aerospace manufacturing companies that will be eligible for such incentives.

Moreover, it is not disingenuous to suggest that Airbus is eligible for the same tax treatment. All aerospace manufacturing companies in Washington, including those from Europe, were treated equally. This point was made abundantly clear to European Aeronautic Defence and Space officials when they were considering Washington as a location for an engineering site and a potential military-tanker modification facility. I made precisely this point to European officials and aerospace companies at the Paris Air Show last month.

Christine Gregoire
Governor, Washington state
Olympia

SIR – You say that American defence contracts are much more lucrative than European defence contracts. However, you do not mention that BAE Systems and EADS, the parent companies of Airbus, have combined defence revenues greater than Boeing's, and that BAE is one of the top suppliers to the Pentagon and therefore a major recipient of this alleged largesse. And while you rightly point out that Europe's defence spending is but a fraction of America's, the money that Europe does not spend on defence contributes to it having the means to substantially increase its funding for aeronautical R&D, largely to the benefit of Airbus. It would appear that Europe wants it both ways—on the one hand it is very actively pursuing, if not demanding, greater access to America's defence market, and on the other it provides government subsidies for the development of commercial aircraft, limiting the size of its own defence market.

Ted Austell
Vice-president for international trade policy, Boeing
Washington, DC

A proper property market

SIR – Housing markets, like most markets, have self-correcting forces that guard against the sort of meltdown that you project ("After the fall", June 18th). When home prices rise too rapidly, consumers do what they've been doing for generations—they simply back away from the market. Many will postpone their decision to buy a home, others will buy a home that costs less and still others will negotiate a better deal for themselves. As sales slow, appreciation rates will settle down or even fall back a bit, giving incomes a chance to catch up with home values and giving builders a chance to catch up in supply-constrained markets. But to argue, as you did, that housing prices will tumble and start a worldwide recession is nothing short of hysteria.

Jerry Howard
National Association of Home Builders

Washington, DC

SIR – You say "It is true that house prices do not plummet like a brick". That may not always be true. In Calgary, prior to the 1983 recession, house prices had been rising as they are now. In September 1983 my home had been valued at C$265,000. I put it on the market, but by December of that year prices had dropped by maybe 40%. My home finally sold in July 1984 for C$131,000. That 50% drop in value happened in just a few months and my home was one of thousands in the same position. There were many expensive homes that became vacant when the equity was so negative that the owners just walked away. It was only in 2000 that house prices recovered. Even today, I could still buy that same house for less than C$265,000.

Larry Romanoff
Calgary, Canada

SIR – October 1929. Professor Irving Fisher of Yale University: "stock prices have reached what looks like a permanently high plateau." June 2005. Harvard University's Joint Centre for Housing Studies: "in several metropolitan areas...natural or regulatory-driven supply constraints may have resulted in permanently higher prices." Enough said.

Nick Whittome
Montreal

Texas's Kinky spirit

SIR – I was disappointed at your depiction of Kinky Friedman as the "obligatory wacky candidate" in the Texas governor's race ("Grandma v the governor", June 25th). Mr Friedman is a passionate Texan who is taking this race very seriously by bringing issues to the public eye that other candidates steer away from and by offering remedies for the ailing state education system. He intends to recapture the proud, wonderfully independent spirit of Texans (he says that cowboys should not be ridiculed) and so restore a positive image of Texas to the world.

Kate Gunn
Houston

The right to criticise

SIR – The British government's long overdue proposal to prohibit incitement to religious hatred does not undermine the "positive need to protect people's right to criticise religions", as opponents of the legislation claim ("Silence, blasphemers", June 25th). The new law will not prohibit anyone from offending, criticising or ridiculing faiths. The attorney-general, Lord Goldsmith, has clearly said it is "about protecting people from hatred, not faiths from criticism". Indeed, under the proposals any prosecution would have to pass the public-interest test of the Crown Prosecution Service and have the consent of the attorney-general. Of the more than 80 race-hate cases sent to the CPS in the past three years, only four have been approved for prosecution. There is no reason to suppose that the CPS and the attorney-general will be any less strict in their interpretation of the new law.

Inayat Bunglawala
The Muslim Council of Britain
London

A fuss over nothing

SIR – Charlemagne proposes to institute a Louis XVI prize, for European leaders out of touch with reality, dedicated to the *Rien* written in the king's diary for July 14th 1789, the day the Bastille was stormed (June 25th). However, this imputes an attitude to the unfortunate Bourbon that simply cannot be deduced from this one-word entry. Madame de Staël, who, as the daughter of Louis XVI's finance minister, was certainly in a position to know, explained in a letter to Gustavus III of Sweden that, in the language of the French court, *rien* merely meant that the king was staying in his own apartments that day.

However, if Charlemagne wishes to pursue the idea of instituting prizes for politicians based on historical chestnuts, why not a Nero prize in honour of leaders that continue to fiddle while the city burns down?

Gerard McKay
Rome

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Clarification: Miguel Petit

Jul 6th 2005
From The Economist print edition

In our issue dated June 25th we published a letter from Juan Miguel Petit that left out Mr Petit's official job title as “Special Rapporteur on the sale of children, child prostitution and child pornography” to the UN. (This has been corrected online.)

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Terrorism

London under attack

Jul 7th 2005
From The Economist print edition

After the joy of winning the Olympics, evil came swiftly

Getty Images

ONCE it had happened, it produced an awful feeling of inevitability. The series of terrorist attacks on London's Underground and bus system at the end of the morning rush hour on July 7th were presumably timed to coincide with the opening meetings of the G8 rich-country summit in Gleneagles in Scotland. The fact that less than a day earlier London had been filled with jubilation at having won the race to host the 2012 Olympic games may have given the perpetrators an extra dose of satisfaction. We shall never know, but nor, actually, should we care. Such a pointless display of brutality should instead bring forth two thoughts. One is that the surprise should be that this has not occurred sooner. The other is that such attacks should not, and will not, make any difference to the way Londoners live and work.

As soon as the atrocities of New York, Washington, DC, and Pennsylvania took place on September 11th 2001, London was assumed to be at risk of attack. That was so both because of its status as an international financial centre, an epitome of the West and its capitalist ways, and because Britain has long been a close ally of the United States, enemy number one for al-Qaeda and its terrorist associates. That likelihood only grew following Britain's participation in the invasion of Iraq in 2003, and then the terrible bombing in Madrid on March 11th 2004. In recent years every senior British policeman, intelligence chief or home secretary you cared to ask about the probability of a terrorist attack gave a similar answer: 100%.

One theory as to why it has taken so long might be that al-Qaeda moves in a very measured, careful way: attacks are long in preparation and intermittent in nature. Yet there is much evidence to suggest that that notion, which became conventional wisdom after September 11th, may not be correct. The intelligence services in London say that they have thwarted quite a number of attacks in recent years, including a plot involving deadly poisons and another which had Heathrow airport as its target. Less encouragingly, they also offer unofficial estimates that Britain may be home to roughly 1,000 budding Islamist terrorists, or close supporters of them. Whatever the accuracy of either of those assertions, the general picture is one of repeated terrorist efforts rather than measured, intermittent ones, and of a fragmented, unco-ordinated set of terrorist groups rather than a cohesive effort.

The apparent leaders of that un-cohesive effort, those who are thought to be the central command of

al-Qaeda, have anyway been in hiding and retreat. There is no way of knowing for sure, but it seems plausible given the number of arrests and killings of people said to be senior al-Qaeda officers—particularly in Pakistan, Saudi Arabia and elsewhere in the Middle East—that the group now has much less of an infrastructure than it did before September 11th and a central leadership that is much less commanding. What it does have, though, is a large group of sympathisers, some with extra levels of motivation since the Iraq war. George Bush has sometimes claimed that a silver lining to the cloud his forces are struggling through in Iraq is that at least the West's enemies are being fought there rather than at home. The attacks in London are a reminder that that view is as wrong as it is glib.

What the attacks also show, however, is that well co-ordinated though the four explosions were, they were not terribly effective. Chance plays a big role in such attacks. The bombs in Madrid last year which killed 191 people might have killed many more had the station roof collapsed. The September 11th hijackings might have killed fewer than the eventual 2,752 had the twin towers of the World Trade Centre not melted down and collapsed. As *The Economist* went to press, the toll in the four London bombs was not clear, but the estimate of at least 33 deaths was thankfully far smaller than in Madrid. By the terrible calculus of terrorism, the attacks should thus be counted as a failure—a sign of weakness, not strength.

Cities vulnerable, cities resilient

The tighter security that has been in place in London since September 11th may have contributed to that. No city, however, can stop terrorists altogether. What can be said, though, is that terrorists are unable to stop cities, either. Perhaps an army, launching wave after wave of attacks, might succeed in doing so, especially if it were to deploy biological, chemical or nuclear weapons. Short of that, cities will always bounce back quickly, after the initial shock. They are resilient organisms, with powerful social and economic reasons to shrug off terrorism. New York and Madrid both show that, triumphantly.

The same will certainly be true of London. Like all large modern cities it is vulnerable to disruption. Millions of people pour into or through the city every day, through its huge transport network, making it easy to identify places to plant bombs and propagate fear. But that also makes the city adaptable. And there is no doubt that the experience of being attacked is likely to make Londoners more determined to resume their normal lives, not less. That would be true even if London had not previously endured decades of attacks from Irish terrorists, but that history makes resilience an even safer bet.

Might the attacks affect Tony Blair's ability to keep British troops in Iraq—presumably the terrorists' goal, if they are indeed related to al-Qaeda? Again, the answer is that the attacks will either prove irrelevant to that policy or, in fact, strengthen both his resolve and his popular support. They may be irrelevant because there is anyway little political or popular pressure for withdrawal of the 8,500 troops that are still in Iraq, even though a majority now believes that the war was a bad idea in the first place. Casualties have been light ever since the end of the formal hostilities, the British are in a relatively calm area of the country, and the public seems to think they are doing a necessary job.

Far likelier, the attacks will reinforce the case for pressing on with the long-term task, as defined by Mr Blair: the establishment of a stable democracy in Iraq, peace between Israel and Palestine, and democratic reform elsewhere in the Middle East. If that sounds rather close to Mr Bush's policy, that's because it is. No terrorists can change that.

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The Supreme Court

The battle begins

Jul 7th 2005
From The Economist print edition

Await the contest with trepidation, but don't pre-judge it

AFP

Get article background

SO ONE of them did go, but not the one everybody expected. For months, the American political world has been girding itself for the resignation of William Rehnquist, the Supreme Court's conservative chief justice, who has cancer. Instead, it was Sandra Day O'Connor, the court's first female justice and its swing-voter on many issues, who announced her retirement after the court ended its summer session.

This caught most of Washington, DC, on the hop—but not for long. Within hours, culture warriors from both the left and the right were making pre-emptive strikes against possible nominees (see article). As much as $100m may be spent in the coming battle. George Bush has appealed for calm, saying that he will take a few weeks to make his choice. He is right to consider the decision carefully: it could be one of the defining moments of his presidency.

In praise of O'Connorism

Justice O'Connor, acclaimed as the most powerful woman in America, will be a hard act to follow. The fact that her retirement is now most mourned on the American left shows how much American politics has turned to the right. Nominated in 1981 by Ronald Reagan as a conservative jurist from Republican Arizona, she helped put the current president in the White House by siding with the majority in the case of *Bush v Gore* in 2000, and she remained a fairly steadfast defender of states' rights, free markets and private property. But on social and cultural issues, her trademark was moderation: she upheld *Roe v Wade*, but accepted some limits on abortion; she struck down some forms of affirmative action, but not others; she had a complicated view on where the line between church and state should be drawn; and so on.

This made for a mixed record in terms of individual decisions. This newspaper would happily have tossed affirmative action, like all other racial preferences, in the dustbin. But, in general, her brand of small-government conservatism and social liberalism reflected the western creed of the president who first appointed her. Justice O'Connor was a useful pragmatist in an increasingly ideological age: she

helped stabilise the court, preventing it from lurching too far from public opinion. Rather than coming to cases with a preconceived set of ideas, she tried each on its merits.

From this perspective, Justice O'Connor is not a bad model for Mr Bush to follow. That is not to deny him the opportunity of choosing somebody more socially conservative than she was; that is one of the perks for the Republicans that accrue from their control of both the presidency and Congress. Mr Bush promised in 2004 to nominate justices in the mould of Antonin Scalia, the court's most articulate conservative. But even conservative jurists come in many varieties, from the hard ideology of Justice Scalia and Clarence Thomas to something a little more flexible.

Mr Bush, who has said he will interview the prospective candidates himself, has always insisted that he has no litmus test, other than that the judge should “faithfully interpret the constitution”. That is a little less pragmatic than it first sounds: some radical conservative jurists hold that liberal judges have not faithfully interpreted the constitution, so their rulings (including *Roe v Wade*) should be reversed. But there are also plenty of conservative judges who are extremely reluctant to change previous rulings, on the simple principle of leaving alone what is already decided.

Hold back those swords

In the meantime, the two sets of culture warriors, currently buckling on their armour, could also usefully study Justice O'Connor's virtuous moderation. Social conservatives, currently acting as if they enjoyed a veto over any selection by the president, seem to have forgotten that on many issues, including abortion, they do not represent a majority (moral or otherwise). They may be stirring up a reaction even within the Republican Party. Certainly, their pre-emptive attacks on Alberto Gonzales, Mr Bush's attorney-general (whom they deem less than sound on abortion) seem merely to have irked the president, who has already expressed his anger over the assaults on one of his oldest friends in politics.

For liberal America, too, there is a clear danger of over-reaching. Talk of Democratic senators filibustering anybody whom Mr Bush puts up sounds nonsensical—not least because it will, as usual, be very difficult to determine exactly what the nominee believes, and because the Democrats, who are currently blocking all they can in Congress, are in danger of becoming a party of pure negativity. In any case, even with Justice O'Connor gone, there would seem to be a clear majority on the court in favour of maintaining *Roe v Wade*.

The Democrats first injected the poison into Supreme Court appointments when they savaged the nomination of Robert Bork, one of conservative America's smarter jurists, in 1987. Mr Bork's America, claimed Senator Ted Kennedy in a notorious piece of grandstanding, was “a land in which women would be forced into back-alley abortions, blacks would sit at segregated lunch counters, rogue police could break down citizens' doors in midnight raids, children could not be taught about evolution.”

Mr Kennedy, who still sits on the Senate Judiciary Committee, might usefully reflect on the fact that, since then, moderates have turned against his party in many of America's culture wars. It could well be in the senator's partisan interests if the Democrats showed they could refrain from knee-jerk “Borking” this summer; it would certainly be in the interests of his country.

Judging by the senator's bellicose language so far (and that of his equivalents on the right), that is probably, alas, a vain hope. Whichever way Mr Bush turns, he is in for a fight that will distract America for most of the summer. In all probability, both sides will dislike whoever he nominates. They should remember that Supreme Court justices are intelligent, independent and seldom as predictable as either Congress or the president like to suppose.

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Mobile phones and development

Less is more

Jul 7th 2005
From The Economist print edition

Mobile phones can boost development in poor countries—if governments let them

iAfrica

Get article background

IMAGINE a magical device that could boost entrepreneurship and economic activity, provide an alternative to bad roads and unreliable postal services, widen farmers' access to markets, and allow swift and secure transfers of money. Now stop imagining: the device in question is the mobile phone. Not surprisingly, people in the developing world are clamouring for them, and subscriber growth is booming. The fastest growth rates are to be found in Africa, albeit from a low base. Already, 80% of the world's population lives within range of a mobile network; but only about 25% have a mobile phone.

The primary obstacle to wider adoption is the cost of handsets. In the rich world, these typically cost around $200 (though most pay less than this thanks to subsidies from network operators), or less than 1% of the average income per person. In the developing world, in contrast, a $50 handset would account for 14% of the annual income of someone earning $1 a day. So the first step in promoting the adoption of mobile phones, say operators in developing countries, is to reduce the cost of the handsets. Several such schemes are under way: in particular, several operators in developing countries have joined together to aggregate their buying power, and Motorola, the world's second-largest handset-maker, has agreed to supply up to 6m handsets for less than $40 each (see article). There is already talk of prices falling below $30 next year.

Industry observers believe cheaper handsets could expand the market by as many as 150m new subscribers a year. As well as boosting economic development in poor countries, this will help to close the “digital divide” between the communications-rich and communications-poor. Governments, you would have thought, would be doing everything in their power to promote the spread of mobile phones.

But rather than treating mobile phones as an important tool for development, many governments see them instead as an opportunity to impose hefty taxes and milk a fast-growing industry for all it is worth. In both Turkey and Bangladesh, for example, anyone buying a new mobile phone must pay a $15 connection tax. Many countries slap large import duties on handsets and impose special taxes on subscribers and operators. In many cases, these taxes double the cost of acquiring a mobile phone. As handset prices fall, such taxes will become an ever more prominent obstacle to wider adoption.

Governments should reduce these taxes at once. Indeed, by doing so, they can both speed adoption and

increase revenues. High import tariffs discourage legal imports of phones and encourage people to buy them on the black market instead. Reducing such tariffs would boost revenues as legal imports increased. Lower taxes on phone calls would encourage adoption and increase the tax base. It can be done: both Mauritius and India have recently reduced their taxes and tariffs.

Mobile phones have created more entrepreneurs in Africa in the past five years than anything else, says the boss of one pan-African operator. Promoting their spread requires no aid payments or charity handouts: handset-makers, acting in their own interest, are ready to produce low-cost phones for what they now regard as a promising new market. Mobile operators across the developing world would love to sign up millions of new customers. But if developing countries are to realise the full social and economic benefits of mobile phones, governments must ensure that their policies help, rather than hinder, the wider adoption of this miraculous technology.

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German elections

Where Angelas need to tread

Jul 7th 2005
From The Economist print edition

An early German election could boost much-needed economic reform

Get article background

NOW that Chancellor Gerhard Schröder has held, and deliberately lost, a vote of confidence in the Bundestag, Germany's lower house of parliament, the stage is set for an early election, probably on September 18th. It could yet be called off, either by the federal president or by the Constitutional Court. But that would be a shame for Germany—and for Europe. The ruling Social Democrat (SPD)/Green coalition has lost its way and looks certain to lose in September. A new government led by Angela Merkel's Christian Democrats (CDU) offers the best chance of reviving Europe's biggest economy, whose slow growth has blighted the neighbourhood.

Mr Schröder has, admittedly, tried to shake up the economy in recent years, first with his Agenda 2010 set of pension, social-security and health-care changes and then through the Hartz labour-market reforms. But he largely wasted his first term from 1998 to 2002, and made no effort in the 2002 election campaign to persuade voters of the need for changes that might hurt. He has since been hamstrung by left-wingers in his own party, by trade-union resistance, by the opposition's grip on the upper house, the Bundesrat, by his government's unpopularity and by the SPD's losses in state elections—but also by that failure to prepare the voters for pain.

This creates an opportunity for Ms Merkel. She knows that Germany needs more and deeper reforms if it is to prosper again. She is also aware that Mr Schröder and, even more so, German business have laid the groundwork for improvement. Unit labour costs have fallen, profits and investment have risen, Germany is once again the world's biggest exporter. The two big shadows over the picture are unemployment (11.7% in June) and continuing low consumer confidence. A CDU victory in September, if followed by bold enough tax measures and further labour-market and other reforms, could presage a rebound in the economy.

Formula for an iron lady

Yet Ms Merkel is adopting a deliberate fuzziness over reform. She has talked, on the one hand, of the need to do things in a fundamentally different way in Germany; but she has promised, on the other, not to put the country's social model at risk in any way. If she wins in September, her party's control of the Bundesrat, which represents Germany's states, should make it easier to push change through. But it could also leave her beholden to powerful CDU state bosses, and to her Bavarian sister party, the Christian Social Union (CSU), led by Edmund Stoiber. Many in the CDU, and even more in the CSU, are enthusiasts for the country's generous welfare system and for the European social model. It was a CDU-led government that first conceived of co-determination, the now much-disliked system of union representation on company boards.

Ms Merkel's reticence on reform may be merely tactical. First, she has to win in September. Her admirers note that Margaret Thatcher (comparisons with whom she fiercely resists) hardly sounded radical before she came to office in Britain in 1979. An exhausted SPD is now tacking to the left by promising tax increases and no more reform, partly to fend off the rise of a new hard-left party. This new party may well complicate coalition-building after the election (see article). But if a CDU-led government emerges, there is every prospect of its staying in power for eight years. That gives plenty of time to devise and adopt radical measures.

This calculation may turn out to be right. But there are still dangers in not spelling out in advance to voters how much change is needed. Even under a government that controls both houses, Germany's

traditional desire to proceed by consensus will remain strong. Governments in Berlin are always fretful about upcoming state elections. And Ms Merkel will anyway be engaged in a perpetual fight against the soggy statist instincts of many in her own party and in the CSU.

That is why she should use the campaign to make the case for reform. This need not mean a long list of specific proposals, which would run the risk of turning off those voters most affected. Nor should it mean ignoring the poor state of German public finances. But Ms Merkel should still be setting out a stall for lower taxes, a smaller public sector and greater reliance on markets. She needs to lean towards the CDU's would-be coalition partner, the traditionally liberal Free Democrats, more than towards her CSU allies. The risk of losing a few votes is less worrying than the risk that, once in government, she will find her plans for fundamental reform once again stymied by a failure to prepare the voters for change.

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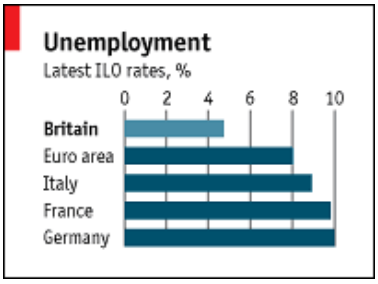
British economy

A cut above

Jul 7th 2005
From The Economist print edition

Britain's economy is weakening. But it still holds lessons for the rest of Europe



HOW many other European governments would have entertained the possibility? In April, halfway through an election campaign, Britain's Labour government allowed the country's last volume carmaker to go bankrupt with the loss of some 4,000 jobs. Remarkably, apart from a few grumbles, most of the nation seemed to think that was just fine.

A prominent manufacturing collapse might seem an odd measure of economic success, but the popular consensus that workers at MG Rover and its suppliers could find jobs elsewhere was a vote of supreme self-confidence. London's victory this week in the race with Paris and other cities to host the 2012 Olympic Games (see article) will no doubt add to that confidence. The facts, though, are less cheering: the British economy has rapidly lost steam, with a sharp downward revision in GDP growth, fears that consumers are deserting the high street, a shaky housing market and fragile manufacturing. On Thursday the wise heads on the Bank of England's monetary policy committee, charged with setting interest rates, left them unchanged at 4.75% (see article) despite noisy demands from the head of the CBI, Britain's employers' federation, for an immediate cut. All the same, it looks only a matter of time before they make a cut—the first in two years.

This slowdown—it is still far from being a recession—comes at an awkward moment for the economy's ultimate guardians, Tony Blair and Gordon Brown. In their calls for structural reform in the European Union, the prime minister and his chancellor have derived much of their authority from the economy's success in generating jobs and wealth. Yet, as things stand, France could be growing faster than Britain by next year. The risk is that, as the cycle turns against Britain, the enduring lessons of its economy begin to fade.

Credit, where it's due

The recent weakness comes after a decade and more in which Britons have had plenty to celebrate. In that time, the country has enjoyed unbroken growth, low inflation and, latterly, joblessness at a 30-year low of 4.7%. By contrast, the eurozone has struggled to slough off slow growth and, in France and Germany, unemployment of roughly 10%. The country that 20 years ago was the sick man of Europe has seen GDP per person surpass that in France, Germany and Italy.

But pride can easily sour into smugness. Much of Britain's growth over the past six years has come not from some national miracle, but from a one-off boost that has raised government spending by five percentage points to an almost continental European 42% of GDP and a splurge in consumer spending on the back of a housing boom that, mercifully, now seems to be abating. A gentle slowing in the economy today is the best way of avoiding a more violent slowing later.

That is one lesson: if Britain's growth is to be rapid and lasting, the country needs to raise its productivity faster. This remains low partly for the admirable reason that the country employs more unskilled workers than, say, France, where they remain out of work. But only partly. Next to its European counterparts, British business is less innovative, employs less capital and draws on a less competent workforce. The ever-larger public sector is even more impervious to efficiency gains. Mr Brown, who has made productivity his thing, has tinkered with grants and education and incentives, but has little to show for it except even more complication for British companies that already complain of overregulation.

Britain has also gained from a sensible monetary policy. This week's decision by the Bank of England was preceded by much speculation of a cut: the markets believe it has the independence and policy framework to safeguard the economy. Compare that with the European Central Bank, also independent, but which has been constrained by the need to set interest rates for a group of divergent economies and is under attack from politicians who accuse it of keeping money dear in an attempt to force structural reform upon them.

But Britain's greatest example comes from the labour market, which still bears the mark of long-past Conservative reform. The changes in union law, the privatisations and the curbing of unemployment benefits seemed harsh at the time. The country at first suffered civil strife, unemployment and strikes—the antithesis of the “social Europe” so many continental leaders cling to. Britain's reforms took time, but they endured and created the conditions for the economy's most striking feature: a capacity to sustain high employment without inflation. There's nothing unsocial about that.

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The Philippines

Gloria in profundis

Jul 7th 2005
From The Economist print edition

Though Gloria Macapagal Arroyo will probably survive, her presidency is now compromised

EPA

Get article background

WHAT are we to make of a president who, allegedly, called an election commissioner at least 13 times in a two-week period during the lengthy counting of votes that resulted in her re-election last year, in one notorious exchange asking whether she would get the million-vote majority she was after and being reassured that “we will try for that”? Interfering in an election would be a very serious charge. If she cannot rebut it, in a self-respecting democracy Gloria Macapagal Arroyo would surely have no option but to resign. Yet that seems an unlikely outcome. So is democracy in the Philippines simply a bad and often-told joke?

At the very least, Mrs Arroyo has some explaining to do. Yet so far she has neither confirmed nor denied that the voice on the telephone intercept that is now causing all the trouble is hers. She has merely admitted to having made a “lapse of judgment” in calling “an election official”—without saying whether that official is the one on the tape. If this all sounds curiously like the twisted legalisms employed by Bill Clinton during his own impeachment calvary, perhaps that should be no surprise. Mrs Arroyo and he studied law together at Georgetown University in Washington, DC.

The problem for the Philippines is that no one seems to be trying very hard to get to the bottom of this murky saga. True, an impeachment motion has been filed in Congress, and will be debated when that body resumes work at the end of the month. But public and political outrage is muted—in the case of the political sort, because Mrs Arroyo's supporters are strong enough to ensure that any impeachment motion has little chance of success. Resignation, removal or yet another revolution (after those of 1986 and 2001) all seem equally unlikely (see article). One reason is that, whatever the proprieties of the case, Mrs Arroyo's explanation that she was anxious to make sure that the other side was not stealing her votes is not entirely implausible. No one really thinks that her interventions, if that is what they were, actually swayed the outcome of the election. Nor is there an alternative president a quarter as well-qualified as Mrs Arroyo waiting in the wings.

This is hardly democracy's finest hour in the Philippines, yet there are some positive points to be made. The most important is simply that the scandal has come to light, has been vigorously debated in the media and in Congress, and has plainly chastened Mrs Arroyo. She has been badly weakened as a result, and will find it harder from now on to push unpopular measures through. She has even, because

of different accusations swirling around him, been forced to send her husband into exile in America. It is not difficult to name a fair few Asian countries where far worse things go on, but where the chances of seeing them even mentioned, let alone debated, in public would be slim.

What is more, impeachment processes, even in a country as proudly democratic as America, tend to be highly partisan affairs, so it would not be surprising if this one goes nowhere. It is also worth remembering that those doing the impeaching, whether in America or the Philippines, are elected politicians, who have their own hides to think of. Few will want to commit political suicide, which is a way of saying that the reason Mrs Arroyo will probably survive is because ordinary Filipinos want her to.

A costly lapse

They support her because she has been a competent and dogged president who has tried hard to grapple with the country's single biggest problem: a chronic budget deficit caused by spiralling demands on an unreformed and hopelessly inadequate revenue base. Mrs Arroyo recently forced Congress to pass two revenue-increasing measures, the first for seven years (though one has just, dismayingly, been struck down by the Supreme Court). After the dismal populist rule of her predecessor, Joseph Estrada, Mrs Arroyo has at least been trying to haul the Philippines back from the brink.

Indeed, the real tragedy of the alleged vote-rigging scandal is that it looks as though, in order to be sure of an election she was always likely to win, Mrs Arroyo has hobbled what remains of a reasonably promising presidency.

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The Srebrenica massacre

A chronicle of deaths foretold

Jul 7th 2005 | SREBRENICA
From The Economist print edition

AP

As the tenth anniversary of the Balkan war's ghastliest episode is remembered, some hard questions still remain for the western powers

LIKE all monuments to great pain, the memorial and cemetery at Potocari, on the north side of Srebrenica, have an aura of their own. Their desolate dignity transcends every attempt to use them for political point-scoring. In the long, flat expanse of a former cornfield, with verdant hills rising on either side, lie a small flower-bed, a simple, open pavilion topped by a tiny Islamic crescent, and a plain stone slab inscribed with a Muslim invocation: “May revenge be turned into justice, may mothers' tears be turned into prayers that there should be no more Srebrenicas.”

Then there are the graves: about 1,300 of them so far, and space for many more as bodies are exhumed and identified. Rough mounds of earth, each with a tapering green headstone, with a name and date of birth: horribly often, the victims are teenage boys. Not many graves bear flowers, or signs of recent tending. In this place, where every other woman lost a husband, a father, and often several sons, most of the bereaved now live too far away (in Sarajevo, or even America) to come often.

In the coming days, the cornfield will be thronged with people. Not only the families of the dead, but also dignitaries from all over the world will mark the tenth anniversary, on July 11th, of Europe's worst mass-killing since the second world war: the murder of up to 8,000 Muslim men and boys by Bosnian Serb forces, overseen by their commander, General Ratko Mladic. (The war-crimes court in The Hague has indicted 19 people for the massacre in Srebrenica, including General Mladic, one of three suspects who has so far eluded capture.) After the speeches at the cemetery, the important guests will disperse, and relatives will start digging a fresh round of graves for newly identified remains.

This hitherto tranquil area grabbed the world's attention in mid-1992, when Serb forces swept across east Bosnia, expelling, capturing or killing the non-Serbs in their path. Srebrenica was one of six towns which the United Nations, in a fudged response, vowed to keep safe and demilitarised. The town's capture by the Bosnian Serbs on July 11th 1995, followed by the slaughter of men and boys over the next five days, marked the end of a ramshackle UN peacekeeping operation and ushered in the final phase of the war, in which the Serbs were driven back to a point where peace terms seemed conceivable.

The region remains sullen and depressed. Its population is now about 10,000, down from 37,000 before the war: 6,000 are Serbs (some displaced from other parts of Bosnia) and 4,000 Muslim. Most Muslims

are recent returnees to farms or flats from which they were ousted in 1992. Many of the area's villages were ruined by war and may never revive.

Muslims and Serbs continue, too, to nurse diametrically opposing versions of history. Take, for example, the nearby village of Kravica. In Muslim memory, the place is notorious because of an agricultural warehouse where, in July 1995, scores of men were killed with bullets and grenades. This was one of at least half a dozen places—along with a soccer field, a school, a quiet riverside, a bend in the road—where mass executions took place between July 12th and 17th. But local Serbs remember Kravica for a different reason. There, in January 1993, on the Orthodox Christmas Day, Muslim forces killed at least 30 people, some say 100. In deep denial of the crimes committed in their name, and dismayed by the world's apparent indifference to their own losses, they are erecting a concrete cross to commemorate their Christmas massacre.

The mayor of Srebrenica, Abdurahman Malkic, a young, jaunty Muslim politician, appears free of personal bitterness, despite his own narrow escape from death in 1995. He too, however, seems doubtful whether this bit of Bosnia can ever revert to its pre-war state. As he grumbles, only a fifth of the region's industrial capacity (based on mining, timber and food processing) is now being used. And it is hard to imagine that this can ever again be the sleepy, moderately prosperous land of hills and lakes where Christian and Muslim youngsters prayed separately but could still fish and flirt together.

Srebrenica's present doldrums are a microcosm of Bosnia as a whole, whose peace settlement imposes a dauntingly elaborate structure to balance ethnic interests. The town is part of the Serb republic (RS) which comprises just under half Bosnia's land, leaving the rest to a federation dominated by Muslims and Croats. Despite the efforts of Bosnia's international overlords, the pan-Bosnian institutions (grouping both the federation and the Serbs) are relatively toothless. As a place led locally by Muslims, Srebrenica gets little aid from the RS, and the other levels in Bosnia's hierarchy have no power to help.

Reliving horrors

In Srebrenica and the area north of it, almost every building tells a story. Many remain wrecked, or scarred by bullets and shells. Opposite the cemetery is the notorious car-battery factory which served as a base for 600 Dutch soldiers wearing the blue helmets of the UN. That was where thousands of terrified townsfolk headed on July 11th after the town was captured by the Serbs.

Reuters

Footage of hell

A few miles to the north lies the town of Bratunac, then and now a Serb stronghold. The Hotel Fontana is still doing decent business. That is where Serb generals engaged in ruthless, deceitful exchanges with Bosnian and UN leaders—with some captive Dutch soldiers sitting nearby to concentrate people's minds.

Thanks to hundreds of hours of testimony before the war-crimes tribunal in The Hague, it is now possible to piece together the outlines, at least, of what happened in these places. Momir Nikolic, a senior Serb soldier, has given a succinct and plausible version of events. On the morning of July 12th, he attended a meeting outside the Fontana with some fellow officers who told him what was now proposed:

> The thousands of Muslim women and children in Potocari would be transported out of

> Potocari towards Muslim-held territory, [while] the able-bodied Muslim men within the crowd of Muslim civilians would be separated from the crowd, detained temporarily in Bratunac, and killed shortly thereafter.

Once the task had been made clear, certain details had to be discussed: where in Bratunac to keep the men before their execution, and then where to kill them. Nikolic suggested two schools and a hangar as detention centres, and for the killings he proposed a factory and a mine.

So much for the 2,000 or so men who were part of the crowd that was foolish enough to place itself under Dutch protection. The remainder of Srebrenica's victims were members of a 15,000-strong group of men and boys who began a desperate walk out of the town on the night of July 11th, once it became clear that the expected NATO bombs would not come.

AP

A continuing task

Using many tricks (including putting on stolen Dutch uniforms, which convinced some Muslims they were surrendering to the UN), the Serbs managed to capture several thousand of these fleeing men—and then kill them.

In mitigation, it is sometimes pointed out that over the previous three years the Muslim defenders of the enclave had made many forays into Serb villages, killing hundreds of people. These raids were led by Naser Oric, a local warlord who now faces war-crimes charges.

Hence, people argue, there was a strong desire on the part of ordinary Bosnian Serbs to take revenge for these killings. That is true, but it does not take away from the monstrosity of the Srebrenica slaughter. Far from being a flash of rage, the murders were ordered and carried out in a clinical, almost industrial manner—and filmed, for good measure. Then, in September, there was an equally well-organised operation to cover up the crime by burying the remains in fresh graves, sometimes breaking the bodies in the process. In the words of Jean-René Ruez, a French investigator, “The massacres took place over three days, July 14th, 15th and 16th, in a perfectly organised procedure, and on July 17th, all the graves were filled in.”

The horrors of Srebrenica accelerated a series of diplomatic and military events that brought the conflict to an end. Three weeks after the massacre, Croatia's American-trained army drove rebel Serb forces (and over 150,000 Serb civilians) out of its territory. That helped free the town of Bihac in north Bosnia from a Serb stranglehold. In late August, NATO began three weeks of air strikes against the Bosnian Serbs, while British and French artillery pounded Serb positions. That helped Bosnian forces break the siege of Sarajevo and, in partnership with Croat forces, roll back the Serbs until their share of Bosnian land had been cut from two-thirds to about half. For westerners, what followed Srebrenica seemed to change a vicious circle into a virtuous one.

The haunting questions

Yet wide-open questions remain about the massacre. Above all, could it have been avoided? To those who were closely involved, the Srebrenica events were in some respects a ghastly surprise, in other ways entirely predictable.

For the previous three years, the world's response to the Bosnian war had been an elaborate effort to dampen the fighting and mitigate its effects without actually intervening. This took the form of a UN operation which policed local ceasefires and distributed aid: a mission which had its own logic, and undoubtedly saved lives, but could not go on indefinitely. In spring 1995, signs appeared that a ruthless end-game was about to begin.

Radovan Karadzic, the Bosnian-Serb leader (who is also wanted for war crimes by the tribunal in The Hague, but has vanished), issued a “presidential directive” calling for an attack on Srebrenica, designed to reduce its size and make life there intolerable. Rupert Smith, the British commander of UN forces in Bosnia, gave a semi-public warning in March 1995 that a stance based on mere peacekeeping would soon become untenable. Realising that the Dutch unit's role in Srebrenica risked becoming worse than useless, General Smith urged the Netherlands to consider two options: either standing firmer in defence of the enclave, or extracting its troops. Neither option was acceptable to the Dutch government.

The UN secretariat, in one of its more honest moments, said the defence of the so-called safe areas would be impossible unless member states contributed more troops. In another telling portent, the Bosnian government itself gave signals that it was open to territorial swaps, as part of a final settlement: for example, Srebrenica would be handed over to the Serbs in return for some other territorial prize, such as the Sarajevo suburb of Vogosca. Perhaps the most mysterious event in spring 1995 was the withdrawal from Srebrenica of its chief defender, Naser Oric.

Yet despite all these omens, the ease with which the town fell to the Serbs amazed even the best-informed of observers. They met no resistance on the ground or in the air. Even a modest show of force by NATO would have saved many lives; and a modest attempt by the town's local defenders to keep the attackers at bay would have bought some time, enough time to shame the world into intervening. Why did neither thing happen? The Bosnians held off from active defence because they thought NATO would provide air support; the UN refrained from seeking NATO support, at least in part, because it feared for the lives of the Dutch soldiers.

The Dutch have reluctantly blamed themselves, and been blamed by others, for failing to use whatever limited room for manoeuvre they had. A similar exercise in self-criticism was undertaken by the UN secretariat, and the diplomats and generals who acted in the UN's name, in the final days of its peace mission.

Whose responsibility?

But placing excessive blame on the UN as an institution is surely to miss the point. Especially in times of acute crisis, the UN tends to lose any collective identity of its own; everyone involved thinks first and foremost as a national of his or her own country. Whatever failed in Srebrenica, it was not the UN but its member governments, which might have intervened to save the menfolk of the town, but did not.

As insiders vividly recall, the Srebrenica crisis triggered a virtual breakdown in the UN's *esprit de corps*: General Bernard Janvier, the French head of UN operations in ex-Yugoslavia, was taking orders from Paris rather than UN headquarters in New York. If the French (both military and political) were reluctant to strike the Serbs, it was partly because they had worked very closely with the Serbian security chief, Jovica Stanisic, to secure the release of French and other UN soldiers taken hostage by the Bosnian Serbs in May. Meanwhile, General Cees Nicolai, the acting UN commander in Sarajevo, was thinking first as a Dutchman, with Dutch lives his main consideration.

Perhaps the hardest question of all is how much western governments knew, and when. The savviest Bosnians will tell you that from the moment Serb forces marched, unopposed, into Srebrenica, it was a chronicle of deaths foretold: an orgy of killing was entirely to be expected, and the Dutch (and other western governments) were being culpably naive when they accepted Serb promises to abide by the Geneva conventions on the treatment of prisoners-of-war and civilians.

If locals relying on their street-sense knew the score so well, how was it that western governments, with their panoply of signals intelligence, satellite photography and military observers, did not know what was going on—and if they did know, why was there such a deafening silence from western capitals during the five days after the enclave's capture, when the massacres were in progress? Is it too conspiratorial to suggest a link between the “usefulness” of Srebrenica's fate, and the fact that it was allowed, over five days, to unfold?

For many Bosnians, there are hard questions not just about the inaction of western governments, but about their own government's weakness of will. As a veteran of the Bosnian army who escaped death

only by scrambling through the hillsides, with four companions, for a terrifying week, Mayor Malkic gives a disarmingly frank answer to these dilemmas. If Bosnian Muslims bear some blame for failing to protect Srebrenica, then the responsibility lies as heavily on people like himself, who were actively involved in its defence, as it does on the Sarajevo authorities. Having said that, “the Bosnian government bears a responsibility that cannot be avoided...[And] of course the main culprits are the aggressors, the Serbs.”

Visiting the cemetery in September 2003, Bill Clinton also gave a remarkably blunt, and politically astute, analysis of the political effects of the massacre. “Srebrenica”, he said, “was the beginning of the end of genocide in Europe. It enabled me to secure NATO support for the bombing that led to...peace.” In other words, without Srebrenica, America could not have won the support of its European allies for a sharp switch to a war-fighting (and thus war-ending) strategy in Bosnia.

On this reading, at least, Srebrenica was a sort of genocide to end all genocides (in one part of the world, anyway). It was also a necessary prerequisite to the dropping of the “bombs for peace”—which, by triggering a final, vast wave of forced population movement, left Bosnia's military balance, and above all its ethnic balance, in a state acceptable to the region's power-brokers.

For the bereaved mothers and widows who gather at the cemetery this week, that surely raises a hard question: was the shock of a massacre the only thing that could make the western powers change policy, and settle their own differences? Was there no other way?

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Correction: mosquito bednets

Jul 7th 2005

In our special report on aid (July 2nd), we said that mosquito bednets, treated with insecticide, “cut the risk of infants dying by 14%, to 63%”. In fact, they cut the risk by 14-63%. This error was corrected online.

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About sponsorship

The attack on London

Murder in the rush hour

Jul 7th 2005
From The Economist print edition

Getty Images

As Britain celebrated gaining the Olympics, terrorists struck London

FOR most of the previous 20 hours, London had been alive with celebrations after unexpectedly winning the contest to host the 2012 Olympic games. But shortly before 9am on July 7th, death and destruction in the biggest terrorist attack in Britain since Lockerbie in 1988 brutally punctured that euphoria. As *The Economist* went to press, police said that at least 33 people had been killed and hundreds injured by three explosions on London's Underground and one on a bus.

That attack blew the roof off a double-decker travelling through Woburn Place in Bloomsbury. On the Tube, eyewitnesses described huge explosions that sent glass flying and filled carriages with acrid smoke. Rescue workers had to use pickaxes to reach trapped passengers. A previously unknown group calling itself the Secret Organisation al-Qaeda's Jihad in Europe said it carried out the attacks as revenge for British “military massacres” in Iraq and Afghanistan—but whether that was any more than gruesome opportunism was anybody's guess.

The attacks knocked out the capital's transport. The entire Tube was quickly shut down—because of a power surge, officials said at first, before news of the explosions filtered through. The mobile-phone network seized up—or may have been switched off to prevent more bombs being triggered. Roads in central London were closed. Trains and coaches heading to London stopped short of the capital. Buses heading to the centre turned round. Those already near the scenes of the explosions became impromptu ambulances, carrying the wounded to hospitals. One Hilton hotel was used for triage.

The attacks seemed planned to coincide with another event: the G8 summit meeting at Gleneagles, in Scotland. Leaders of the big industrialised countries meeting there expressed their sympathy as Tony Blair rushed back to London, after vowing that: “Our determination to defend our values and our way of life is greater than their determination to cause death and destruction to innocent people in a desire to impose extremism on the world.” Ken Livingstone, London's mayor, also denounced the attackers: “even after your cowardly attacks, you will still see people from around the world coming to London to achieve their dreams.”

For officials, the attacks were long-feared, even expected. Since September 11th 2001, London's emergency services and other government agencies, private security services and other business, have attempted to adapt their response to a changed terrorist threat. Where Irish terrorists were expected to

give warning before attacking the capital's infrastructure, Islamic terrorists would remain silent before attempting to inflict mass casualties. Sir Ian Blair, head of the Metropolitan Police, said: “We have planned and prepared for this. A sophisticated emergency operation is swinging into operation.” He urged Londoners to stay where they were. The many who were stranded by the transport system's collapse had no choice.

London's anti-terrorism precautions are among the most elaborate and well-practised in the world. A top spook who briefed *The Economist* last year gave a blood-curdling account of attacks foiled—among others, an attempt to blow up a famous hotel from its underground garage. In 2003 the army patrolled the flightpaths near Heathrow airport, fearing that terrorists had got hold of an anti-aircraft missile. But there was little complacency. “We have to be lucky all the time. They have to be lucky only once,” he said. Such warnings were not always well received. When the previous Metropolitan Police chief, Sir John Stevens, said last year that an attack was “inevitable”, he was pilloried for scaremongering.

A public-private group put together after the attacks on September 11th has reported great improvements in the capital's security and emergency planning. Businesses have employed many more security experts; 6,000 closed-circuit cameras are now distributed widely across the Underground system; £56m ($98m) has been committed to Britain's capacity for decontamination and a further £132m to improve the fire and rescue service.

But they have also revealed the failure of some government bodies to co-ordinate well—a habitual problem in London, where metropolitan and national police agencies are in constant, sometimes confused, competition. “The government and everyone is cognisant of the new threat, but it is inordinately difficult to deal with,” says Mark Whitaker, deputy director for crisis and security management at Control Risks, a security company. Integrating transport police with the rest of the police and the ambulance and fire services is, he says, “hugely complex”.

Preparation and defence can go only so far. More than a million people were on the move in the rush hour, when the terrorists struck. Each day some 500,000 people commute to central London by bus and more than 2m take the Tube. It is hard to protect such a system from attacks; and, when they happen, they disrupt millions of people's lives.

Yet Britain has seen and survived terrorism before: the IRA's Birmingham pub bombings killed 21; in Northern Ireland, the Omagh bombing in 1998 killed 29. In 1984 an IRA bomb nearly killed Margaret Thatcher and her cabinet. Sustained attack made Britons vigilant: business has anti-terrorism insurance (see article) and citizens these days tolerate more intrusive surveillance. Decades of experience have made Britons resilient.

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London's 2012 Olympics

And the winner is

Jul 7th 2005
From The Economist print edition

The Olympics could change London for the better, but only if the city is hard-nosed

Reuters

Kelly Holmes (centre) and Steve Cram (right) win again

IN THE pursuit of Olympic gold medals, they say, it is not so much the winning but the taking part that counts. In the pursuit of the Olympic games, winning is everything. How sweet, then, for Britons that London this week saw off Madrid, Moscow, New York and the firm favourite, Paris, to stage the 30th Olympiad in 2012, becoming the first city to host the games for a third time.

London can bask in such recognition of its status as a world city, but status isn't everything. The real question is whether hosting the Olympics will actually be good for Londoners. Past experience and current plans suggest that London 2012—which already sounds like an optometrist's diagnosis—might not be.

Parts of London's plan are undoubtedly wise. Temporary stadiums will be put up in scenic parts of London such as Greenwich (for equestrians) and Horse Guards Parade (for beach volleyball). Existing venues such as Wimbledon (for tennis) and Lord's cricket ground (for archery) should be inexpensive and work well.

The problems start with the site of the Olympic complex. London's bid was reckoned to be strong on regeneration, which is another way of saying that its plan called for an enormous amount of new building. The main stadium and the athletes' village will be laid out on a slug-shaped area in the Lower Lea Valley, which despite its picturesque name is a wasteland three miles east of London's financial district that today is scarred by car-breakers' yards and derelict factories. Once home to food-processors and a sewage works, it has absorbed “two or three centuries of industrial abuse”, according to David Stubbs, environmental manager for London's bid. All this will have to be cleaned up (with public money) before any building starts. Oh, and the site often floods.

Optimists point to the regeneration of Canary Wharf as an example of how London can turn an unloved no-man's land into a highly desirable address. But the task over the next seven years is on quite a different scale. Whereas the original Canary Wharf estate was a modest 87 acres, the Olympic park will be 500 acres, a bigger area than Hyde Park.

That means the games will cost a lot. Few Olympics make money once you count the cost of such things as permanent stadiums and new transport links, where London is notoriously weak. The games that have made a profit, notably Los Angeles in 1984, did so by doing as little new building as possible.

Holger Preuss, an academic at Cologne University who has studied the economics of hosting the games, reckons that London's plans are towards the ambitious end of the scale.

The planned public subsidy for the games is £2.4 billion ($4.2 billion), split between the National Lottery, the London Development Agency and council-tax payers in London. But that figure is necessarily rough: nobody knows, after this week's co-ordinated terrorist attack on London, what the security budget will be in seven years' time. As deadlines approach, costs can escalate. The budget for the Athens games started at €4.6 billion ($5.5 billion), but the final price tag is thought to have been almost twice that.

Olympophiles counter that the games justify a large public subsidy by boosting tourism. But, unlike Barcelona in 1992, Seoul in 1988 or Tokyo in 1964, London in 2012 has no need to be put on the map. Stefan Szymanski, an economist at Imperial College's Tanaka Business School in London, reckons that although the Olympics might attract those tourists who like their sport, it will drive away those who come to London for its art and theatre. Set against Britain's £1.2 trillion economy, any direct boost is likely to be tiny.

Others argue the games will create such exuberance that consumers will rush to the shops filled with a desire to buy things. But it is anyone's guess whether an expensive feel-good factor will be what Britain's economy needs in 2012. Portugal made a bid to host the Euro 2004 football championships when its economy was rosy, but ended up paying for it when growth had slowed. That did not feel so good.

To reduce the risk of an expensive mess, London needs to avoid three traps. The first is a habit of mismanaging big public projects, delivering them late and over-budget. This disease has effected the Millennium Dome, the rebuilding of Wembley football stadium and the refurbishment of the capital's execrable Underground. Here the prescription is to settle the final design from the outset, to procure intelligently (not always choosing the cheapest), and to start building as soon as possible.

Second, London's mayor, Ken Livingstone, must be prevented from using the Olympics as a way to extract money from the government for his pet projects. Instead, his task will be to barge through the numerous obstacles to the Olympic plan. One property developer who negotiated permission to build a large development in a neighbouring part of east London says he ended up talking to around a hundred planning and development agencies and their offshoots. Each has slightly different hopes for the Olympic legacy. Pushing the project through on time and on budget will mean ignoring many of them.

Third, between now and 2012 there will be the inevitable souring of the elation at winning the bid. Britain's famously critical media will seize on cost over-runs, higher taxes and, quite possibly, the idea of spending so much money in London—easily the most prosperous part of the country. Of course, Tony Blair, who has won so much praise for fighting for the bid, will be long gone by then. It will fall to his successor to stay the course.

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Interest rates

They're coming down soon

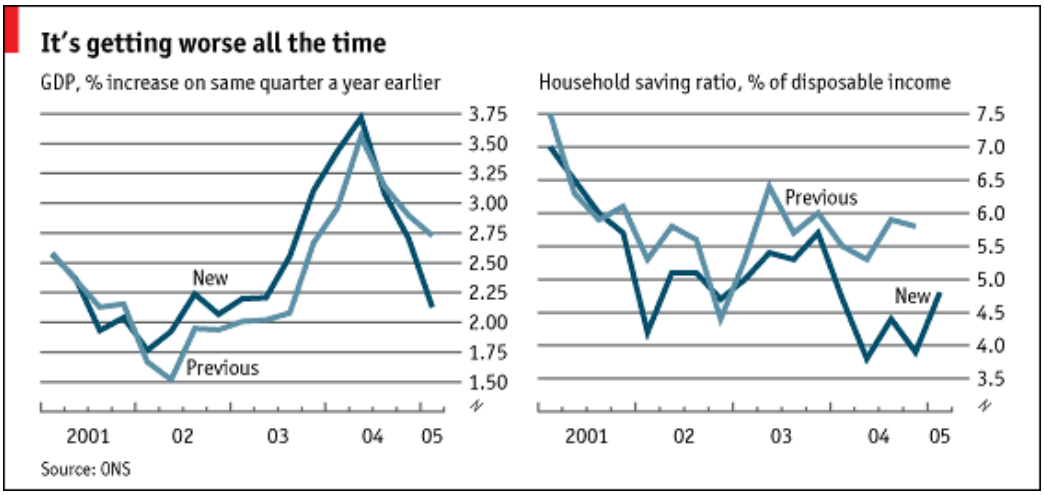
Jul 7th 2005
From The Economist print edition

A weaker economy needs easier money

THE Bank of England kept interest rates on hold on July 7th. They have now stayed at 4.75% for almost a year. But relief for borrowers is at hand. The Bank is expected to lower rates to 4.5% next month and the markets are pricing in a further cut, to 4.25%, by the end of the year.

The swing in monetary mood has been little short of manic. Earlier this year, the City was betting rates would rise in 2005. In March and April, two members of the Bank's nine-strong Monetary Policy Committee (MPC) voted to raise rates to 5.0%; and there was one vote for a hike in February and May.

But when the MPC met in June, the hawks had folded their wings: there were no calls for higher rates. As before, a clear majority voted to keep rates at 4.75%. But two members, including Charles Bean, the Bank's chief economist, turned doves, backing a cut in rates to 4.5% in order to bolster a weakening economy.



Since that meeting, fresh evidence has emerged of an economy that has been even weaker than previously realised. Not for the first time, the Office for National Statistics (ONS) has issued revisions to the national accounts that rewrite recent economic history. They showed that the recovery from the slowdown in 2001 and 2002 had initially been stronger than thought, but lost steam last year to a greater extent (see chart). As a result, the economy grew in the year to the first quarter of 2005 by 2.1% rather than the previous estimate of 2.7%.

Adding to the MPC's worries, the revisions also revealed that the economy has remained unhealthily reliant upon a consumer boom, fuelled by an overheated housing market. The new figures pushed up consumption growth for 2002 and 2003, and raised it last year to 3.7% from 3.3%. The price of this dependence was paid in the first quarter of 2005 when household spending came to a virtual standstill. Whereas the previous figures had shown that consumer spending grew by 0.3%, the new ones showed that it rose by 0.1%, the lowest in over four years.

The Bank has been trying to engineer a deceleration in consumption growth, only to see it collapse—though it is possible to put a more optimistic spin on the new figures. Whereas the previous estimates had shown meagre consumption growth of 0.2% in the final quarter of 2004, the new ones

revised this up to 0.6%. This suggests that the consumer slowdown may be less entrenched than was once thought.

On the other hand, the ONS also revealed that consumers had to run down their savings to sustain their spending last year. Indeed, the saving ratio fell to 4.2% of disposable income in 2004, the lowest since the series started in 1963. The main reason why consumer spending was so weak in the first quarter was that consumers started to save more.

The greater fragility of household budgets revealed by the new figures suggests that the consumer slowdown is likely to persist. That is certainly the bleak message from the high street. The British Retail Consortium reported on July 5th that the value of sales between April and June fell by 2.4% compared with the same period a year before. According to the Confederation of British Industry, which lobbied for a rate cut this week, retail sales fell in the year to June at the steepest rate in its survey's 22-year history.

But that depth of gloom is over-Stygian. The housing market—source both of the earlier strength of consumer demand and its more recent weakness—seems to be stabilising. In May, for the second consecutive month, there were around 95,000 new loans for house purchase, well down on a year before, but up from the low of 77,000 in November.

Another reason not to overdo the gloom is that services activity rose in June according to the monthly purchasing managers' survey. A similar survey for manufacturing showed an upturn, although the sector remains fragile.

These signs of resilience were probably enough to convince the MPC that an early move down in rates was not required. But the strong chance of feeble growth in the second quarter—the National Institute of Economic and Social Research is forecasting a rise in GDP of only 0.3%—means that a cut in August is on the cards. In a poll of economists on July 5th by Reuters, 26 out of 43 said that rates would fall next month.

If the Bank does lower rates in August, this will mean that, at 4.75%, they peaked well below their high in the previous cycle of 6.0%. An important reason for this is that consumers have so much more debt these days, that the burden of servicing it is a heavy one even with relatively low interest rates. Household debt now amounts to 150% of disposable income, up from 110% in 2000. That debt burden, together with a still overvalued housing market, are reasons to worry about the prospects for the British economy even with the salve of lower rates.

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Special schools

Extra-special profits

Jul 7th 2005
From The Economist print edition

Why the state pays for the priciest schooling in the country

SPENDING taxpayers' money on private-sector education is anathema to the educational establishment when it concerns bright children wanting an academic school. But when the child is damaged, disturbed or disabled, it's standard practice, even at £250,000 a place.

This week the Priory Group, best known for its high-profile treatment of celebrities' addiction and depression, was sold for £875m. Its education business—chiefly 18 special schools and 590 pupils, mostly with autistic disorders or dyslexia—contributes just under a third of its £200m turnover. The other main private provider, the Hesley Group, which looks after 390 children in ten schools, is on the block for some £80m—a multiple of more than twice turnover and more than 40 times its 2003 profit of £1.7m.

That seems odd. First, the price tags are startling: for-profit educators normally expect to pay between 10 and 13 times earnings for a school. Second, the state pays for-profit schools the same as their state-run and charitable counterparts. Third, special schools look like a declining market. The educational fashion is to adapt mainstream schools to include as many special-needs pupils as possible.

But that still leaves some children whom ordinary schools cannot, or will not, cope with. Some have multiple disabilities and need 24-hour residential care; others have extreme forms of autism; others have become intolerably disruptive because of mistreatment by parents. Faced with that, a costly special school can seem like a bargain. The (charitable) Mulberry Bush school in Oxfordshire, for example, charges more than £100,000 a year, with which it pays 100 staff to look after its 36 pupils, mostly victims of indescribably ghastly abuse. After three years of therapy, they usually return to mainstream school.

The for-profit providers argue that they are much more efficient than their charitable counterparts. Bob Lewis, director for education at the Priory Group, says a chain of schools allows proper career development for his specialist staff. That sounds convincing: emotionally draining work makes staffing an industry-wide problem.

But the venture capitalists who are moving into the industry also reckon that the long-term prospects are good. Official opinion is shifting against inclusion. Local education authorities are too small to provide specialist education themselves. “Most parents want the best and that isn't to be found in the maintained sector because the investment isn't there,” says Rowie Shaw, an educational consultant.

There is also growing demand for special education from ordinary parents. Alphaplus, the country's largest for-profit schools operator, has just opened a new school in London for young dyslexic and dyspraxic (disablingly disorganised) children. It is aimed at middle-class parents who think the state system is inadequate, but fear that without special coaching, their children will fail to get into the capital's fiercely selective private schools.

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The second world war

VG Day

Jul 7th 2005
From The Economist print edition

Britain celebrates a piece of history that is rapidly dying

AFP

Palace pictures

JULY 10th 1945 passed quietly in Britain. A small parade in London was held to thank civil-defence workers for their contribution to the war effort. “That apart,” says Daniel Todman, a historian at London University, “it was unusually uneventful. You would be hard pushed to find a day with less to commemorate.”

Odd, then, that 60 years later Britain has decreed it the day to remember the entire second world war. Such anniversaries have normally been in May or August, marking victory in Europe and Japan respectively. But both dates are controversial. Big events in May annoy those who fought in Asia; association with the first atom bomb tarnishes festivities in August.

In contrast, a politically neutral date leaves everyone happy. Organising one celebration, not two, also makes good financial sense.

But it isn't just the date that has caused past disagreements. John Major botched the 50th D-Day anniversary when the then prime minister's plans—which included a spam-fritter-frying competition — were judged a poor way to honour the deaths of 7,000 men on the beaches of Normandy. Past rows have flared around invitations to German soldiers, the right mix of “celebrations” and “commemorations”, and veterans' hotel rooms.

This time such snarl-ups have so far been avoided. People can visit a “living museum”, staffed by actors and volunteers in costume, in London's St James's Park. Veterans, meanwhile, will take tea with Queen Elizabeth and watch a special variety show on television.

Elsewhere there are changes to the way the war is remembered. Interest in the first world war, wrongly thought to be unforgettable, waned as its veterans died. Now that “the soldiers of this war are rapidly dying out,” says Sam Haywood of the Imperial War Museum, “time is short.” There is a push to record veterans' memories and tell war stories to youngsters, paid for with £50m from the National Lottery.

The veterans seem happy enough. Eric Reeves, a sergeant in the Queen's Royal Regiment, found it “wonderful to tell children about our experiences. I've been doing it all day.” He isn't bothered by the idea of celebrating halfway between victory in Europe and Japan. “We were in the same war, after all.”

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Congestion charging

Bigger and dearer

Jul 7th 2005
From The Economist print edition

London's congestion charge is a success, but expanding it is controversial

TWO and a half years since its launch, Londoners like their city's crude road-pricing scheme. It has cut city-centre traffic by 15% and congestion by 30%. The re-election last year of its chief proponent, London's mayor, Ken Livingstone, encouraged ministers to float the idea of a national road-pricing scheme.

Cheered by that popularity, Mr Livingstone is increasing both the charge's price and scope. On July 4th, he raised the price of driving into central London by an inflation-busting 60%, from £5 to £8—despite having said in 2003 that it was likely to remain unchanged for a decade. He also plans to extend the zone westward into an expensive residential area (see map).

Transport for London (TfL), which runs the scheme, says that the price rise is needed to "maintain the benefits" of the charge, because inflation and economic growth have made it less of a deterrent to motorists. That argument is not entirely convincing. TfL's own statistics do not show any sign of the deterrent effect weakening. Traffic levels are broadly stable. In any case, officials predict that the higher charge will cut traffic only slightly, by a further two to six percentage points.

The suspicion is that the timing is political. Mr Livingstone may be hoping that voters will have forgotten—or forgiven—the rise by the next mayoral election. A survey carried out by TfL showed the extension to be unpopular with residents. But so, at first, was the original scheme. The mayor says the survey was "not representative"—but he has agreed to extend a 90% price cut for residents to people in the new zone, even though that will boost congestion in the city centre as thousands of motorists take advantage of their discounts.

Businesses claim that the higher charge will further damage shops in the existing zone and that the westward extension will spread the pain. Many Londoners think the congestion charge is badly run by the contractor, Capita, perhaps even deliberately so: penalty charges for late payments account for more than a third of the scheme's income. Officials say that it is unlikely that the efficient automatic payment system used by businesses will be extended to private motorists before 2009.

The real worry is about the purpose of the scheme. In 2002 Mr Livingstone insisted that its aim was to cut congestion, not raise money. When revenues turned out to be much lower than planned, it supposedly didn't matter. Now talk of the need for extra revenue has become louder. The mayor's plans, says TfL, could raise an extra £43m-63m to be spent on public transport, especially more buses.

That is disturbing, since the point of a road-pricing scheme should be to discourage the overuse of an under-priced resource rather than to swell official coffers. TfL refuses to set a target for congestion, leaving plenty of room for politically motivated manoeuvre. The mayor has said that he will not raise the charge again in his current term. But his promises are worth little. And if the public begins to suspect that revenue-raising, rather than congestion-cutting, is driving the scheme's expansion, then support will shrivel.

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Car parking

Fear the meter

Jul 7th 2005
From The Economist print edition

Parking is a money-spinner for local government and it's going to get bigger

“A CAR in every garage and a chicken in every pot” defined progress for Herbert Hoover. Britain now has plenty more cars than garages, and fewer parking places than cars. Their owners are paying more as a result.

Recent figures show drivers now pay more than £1 billion in tickets and fines annually, double the amount ten years ago. Almost half of this is profit for local government. This follows a change to parking rules in 1991 allowing local authorities to take responsibility from the police and give it to private companies, which use targets and incentives to book more offenders. NCP, the biggest parking company, once offered a new car to the warden issuing the most tickets.

The result is a revenue-raising triumph, but a public-relations disaster. Motorists accuse crafty councils of deliberately using parking to top up their incomes. Reports of over-zealous enforcement—including tickets for fire engines, buses and even a rabbit's hutch left on a street corner—have created the belief that vindictive councils are illegally fleecing motorists for cash.

Motorists might be frustrated, but they should in future expect to pay even more to park. For one thing, the new policy is better than the old, in which patchy enforcement encouraged motorists to park illegally, leading to clogged streets. The new system gets more people to pay up and catches more of those who don't. Nick Lester, of the Association of London Government, says most of the money comes not from tickets and clamps but from “more people paying more to park legally”.

In any case, the new parking regime is still growing. To date, around 120 of the 410 councils in England and Wales run their own parking—though this includes the London boroughs. The official body that deals with motorists' complaints expects a further 40, including cities such as Sheffield and Newcastle, to opt in over the next two years. At the same time, the scope of parking enforcement is likely to widen. In 2000 London councils began policing bus lanes, adding roughly half a million extra parking tickets in the past two years.

But the chief reason people will pay more is that they are buying more cars—12m of them by 2030, says the RAC. Towns cannot just conjure up expensive multi-storey and underground garages and new roads lined with parking, so they will charge more instead. Ultimately, out-of-pocket parkers may prefer the disease to the cure: being deterred from taking to the asphalt thanks to heavy road charges.

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Bagehot

A new direction. But which one?

Jul 7th 2005
From The Economist print edition

It is beginning to look as if their leadership contest will present Tory MPs with a real choice

Get article background

THE simmering Tory search for a leader has suddenly become interesting. There are still too many cringe-making jokes about when and when not to wear a tie. But, thankfully, those who want the job are showing signs of wanting to move beyond the bland and the formulaic. Against expectations (Bagehot's included), Michael Howard's decision to allow six months of introspective debate about the party's future before the election of his successor is producing something that may be of value.

It needs to. If there were any lingering doubts that the Tories urgently require a new direction, they were dispelled at the end of last week by Lord (Michael) Ashcroft, a successful, if controversial, businessman and former party treasurer. Lord Ashcroft has published an analysis of £750,000 ($1.3m) worth of polling he privately commissioned covering the seven months up to the election. “Smell the Coffee: a wake-up call for the Conservative Party” is a devastating critique of the campaign the Tories fought.

Part of Lord Ashcroft's purpose is to show how the strategy of targeting 164 seats (the minimum the Tories needed to win to form an overall majority) was absurdly over-ambitious and “a disaster waiting to happen” that only limited their gains. But its most important conclusions for the future relate to the negative way the party presented itself to the electorate.

In particular, the anti-immigration message that was designed to appeal to the reactionary instincts of working-class Labour supporters was a terrible miscalculation. It was never an important enough issue to detach Labour voters from their traditional loyalties. However, as Lord Ashcroft says, it prevented “us from connecting with our real core vote...the election-winning coalition of professionals, women and aspirational voters without whom the party risks becoming a rump.” To underline the warning, a post-election poll gauged the potential support of all three main parties at the next election. It found that 54% of voters say they are potential Labour supporters, 51% potential Liberal Democrats and only 44% potential Conservatives.

Based on the detailed results of his polling (carried out by Populus and YouGov), Lord Ashcroft's conclusion is that the Tory leadership failed to talk about the things that mattered to people and deluded itself about the party's real prospects.

It is against this bleak background that the leadership contenders' words should be judged. Of the ten or so likely candidates, only the Davids—Davis, Willetts and Cameron—should be taken seriously. Although others will remain in the field until the autumn, most will struggle to persuade 20 of their parliamentary colleagues to nominate them. Ken Clarke has the backers to mount a bid, but his fanatical Europeanism, age and uncertain appetite for opposition make him unelectable.

This week Mr Davis made his first big speech since becoming the bookies' favourite to lead the party. The shadow home secretary is on a roll, having won praise for his battering of the government's ID card plans. A YouGov poll in the *Daily Telegraph* on July 4th showed that public support for the cards is plummeting. Mr Davis's confident interpretation of the Tories' disastrous campaign was that a lack of boldness had prevented the party from communicating a clear direction.

He reckons that what has been missing for more than a decade is the kind of Tory radicalism that marked the Thatcher era. Her targets had been over-mighty unions, moribund nationalised industries and punitive taxation. His would be unreformed, cash-gobbling public-service monoliths that fail the people they are supposed to help. His remedy is to take spending power from central government and

put it firmly in the hands of patients and parents, who will be free to buy whatever health care and schooling they want from a variety of eagerly competing providers. By cutting marginal rates of tax, the resulting economic dynamism would generate the additional revenues needed to pay for it all. Such ideas could have come straight from Reform, a fiercely free-market think-tank. In fact, they probably did: Reform's former director, Nick Herbert, the new MP for Arundel and South Downs, is very close to Mr Davis.

Mr Davis's intention is plain. He is sounding a trumpet for politics as ideological combat. Tony Blair's attempts at market-based reform of public services count for nothing. Practical difficulties are brushed aside. Mr Davis has a compass and it is pointing him out into clear blue water.

The compassionate tendency

The contrast with both Mr Cameron and Mr Willetts could not be greater. Mr Cameron thinks it is “crazy” to exaggerate the differences between his party and Labour. He says: “I came into politics to do the right thing” not “to engage in some positioning exercise.” As an example, he cites his support for the government's City Academy programme. And he cautions: “Real modernisation means evaluating ideas and policies on the basis of how they would actually work in practice.”

Both Mr Cameron and Mr Willetts (in a compassionate and lucid speech to the Child Poverty Action Group) are concentrating their thoughts on what can be done to foster a decent society. They believe society is afflicted by family breakdown, rampant individualism, the cycle of deprivation that condemns many people to persistent poverty and the well-meaning but clumsy interventions of a state that often makes things worse. Mr Willetts is dauntingly cerebral, while Mr Cameron is charming and more colloquial. Mr Willetts is widely admired. However, Mr Cameron, who gained the backing of Oliver Letwin a few days ago, is now generally thought to have the better chance of beating Mr Davis, whose support is noisy but not yet deep.

For his part, the perceptive Lord Ashcroft is interested in only one thing: winning the next general election. Which of the Davids would he choose?

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German politics

One country, two governments

Jul 7th 2005 | BERLIN
From The Economist print edition

Gerhard Schröder loses a vote of confidence, but his likely successor, Angela Merkel, is unsure how to campaign

Get article background

HISTORY has made Germans distinctly wary of political experiment. Still, these days they are being treated to a rare democratic spectacle. The country has, in effect, two governments: one that is trying to get out, but may not be allowed to; and another that is likely to get in, but has yet to make up its mind exactly what to do.

On July 1st, Chancellor Gerhard Schröder engineered his own defeat in a vote of confidence in the Bundestag, the lower house of parliament, enabling him to ask the federal president for a dissolution and an early election in September. On July 11th, all eyes will be on Angela Merkel, leader of the opposition Christian Democrats (CDU) and Mr Schröder's likely successor, when she presents her party's "government programme".

This two-headed rule is not quite what Mr Schröder had in mind when he said that he would seek an early election after his Social Democratic Party (SPD) was crushingly defeated in North Rhine-Westphalia's state election on May 22nd. To him, it was mainly an act of self-liberation. Mr Schröder felt boxed in, not only by left-wingers in the SPD and by the opposition, which controls the Bundesrat, or upper house, but also by Germany's dire fiscal situation and a visa scandal. "If we want to release energies and implement further reforms, we must crack the physics of power," he declared enigmatically in his speech before the vote of confidence.

Cracking the physics of power is hard in Germany. In the name of political stability, the country's constitution makes it difficult to dissolve parliament. If a chancellor wants to go to the country, he cannot just engineer a lost vote of confidence; he must, to quote from a ruling on the matter by the Constitutional Court, demonstrate that he no longer has "continuing parliamentary support".

Since Mr Schröder made his decision to call for an early election, Germans have been treated to weeks of speculation over exactly how he would go about losing a vote of confidence. In the end, the SPD's parliamentary group was "invited" to abstain. And Mr Schröder argued that, given mounting internal and

external opposition to his reforms, the “democratic sovereign” should now decide.

The question is whether Germany's president will agree. Horst Köhler will be especially anxious that the Constitutional Court does not overrule him. A few members of parliament have said that they will file a complaint if the president calls an early election. By coincidence, on the day of the vote of confidence, the court issued an opinion suggesting that an election could take place on September 18th “or later”, triggering speculation that the judges might yet order a delay. Yet in practice neither Mr Köhler nor the court is likely to stand in the way, because to do so would be to go against the will of parliament, the main parties and most voters.

Many in the SPD would be relieved if the election were not to go ahead, because the forces unleashed by Mr Schröder have not done the party any good at all. Far from generating new momentum for the government, they have sped its decline, not least by driving a wedge in the SPD's coalition with the Greens. The SPD is now running below 30% in the polls and the party has responded by moving to the left. In some ways, it is already behaving as if it were in opposition. Its election programme, presented on July 4th, boasts such classic left-wing gestures as higher taxes on the rich and a minimum wage.

All this should make life easier for Ms Merkel, the CDU's candidate for chancellor. Indeed, since Mr Schröder's announcement of early elections, Germany has gone through something akin to Merkel mania. In the space of a few weeks, her popularity rating has shot past the incumbent's. The media have taken to her, and even begun printing nicer pictures (a development helped by a makeover, a new hairstyle and more smiles). She was the undisputed star of many of Berlin's summer parties last week.

Yet Ms Merkel would be the first to concede that reality will sooner or later hit back. In fact, where Mr Schröder wants to shatter the “physics of power”, Ms Merkel is trying to contain it. Maybe this reflects her background as a physics professor; to her scientifically trained mind, rationality is important. But she must also fear the fate of Edmund Stoiber, the opposition's candidate in 2002, who unexpectedly lost to a rejuvenated Mr Schröder.

When Ms Merkel presents her programme next week, it will be treated by many as her first big appearance as chancellor-designate. At first, it seemed that she would not spell out tough reforms and budget cuts ahead, to protect herself from attack—a strategy that helped the CDU to victory in North Rhine-Westphalia. Yet this approach has triggered criticism within her own party, and a few calls for her to tell voters the truth.

If insiders are to be believed, the programme will now be more honest. Yet it will not be as straightforward as it should be, because of the constraints operating on Ms Merkel: the budget deficit, diverging interests within the opposition, the SPD's move to the left, a new left-wing party (now called the “Left Party”) and, not least, the prevailing pessimism that makes many Germans want to discount everything that politicians say.

A Chancellor Merkel would probably first try to introduce labour-market reforms, such as reducing job protection. More expensive measures, such as a flat-rate health-care fee and a simpler tax system, will have to wait. To pay for them, the programme is likely to include an increase in value-added tax, from 16% to 18%, and a cut in such tax subsidies as deductions for commuters. To avoid appearing too liberal, there will also be some gestures to demonstrate social balance. Ms Merkel hopes to present all this while sounding simultaneously credible and optimistic.

Which of Germany's two governments will remain standing after the election? It is hard to see a looming war or a natural disaster big enough to save Mr Schröder and his government this time (the prospect of a war in Iraq and a flood in eastern Germany did the trick last time). And it seems all-but certain that the CDU will emerge with the most seats in parliament, even if it does not manage to secure enough for an absolute majority.

Other than this, however, all bets are off. In some ways, the election may be more about Ms Merkel's four-month “tenure” as chancellor-in-waiting than about Mr Schröder's record. In the polls, at least, the CDU seems to have peaked already. And the new Left Party could do better than is at present expected. The latest opinion polls give it over 10%. If these trends hold, it could be difficult for the CDU and its coalition partner, the Free Democrats, to form a majority.

It is thus conceivable that Germany's two governments could be pushed into one: a grand coalition of the CDU and SPD. Would this be good for the country? Opinion is divided, since the only grand coalition tried, in 1966-69, is widely deemed to have been a failure. Some joke that there is only one person who could make such a configuration work as chancellor: Mr Köhler, who has become one of Germany's most popular politicians. Now that would be a new political experiment.

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French politics

Flight from the centre

Jul 7th 2005 | PARIS
From The Economist print edition

The strange similarities between two would-be presidents

AFP

Fabius to the left, Sarkozy to the right

Get article background

AT FIRST glance, Laurent Fabius and Nicolas Sarkozy, two presidential hopefuls for 2007, have little in common. On the left, Mr Fabius is a product of the left-bank intelligentsia and the Ecole Nationale d'Administration, France's civil-service college, who was prime minister in 1984-86. On the right, Mr Sarkozy is no *énarque* but a lawyer with a terrier-like manner, who has been repeatedly passed over for prime minister. Yet the pair have begun to adopt similar political strategies.

Each has started to seduce the political extremes. Mr Fabius's charm offensive began when he ignored a Socialist Party vote for the European Union constitution last year and led a breakaway camp of rejectionists. His fellow-travellers included Trostkyites, revolutionary and ordinary Communists, and anti-globalisation protesters. He posed with José Bové, an anti-capitalist farmer, denounced a Europe "dictated by finance", and promised a warmer, friendlier world. Since the French no vote, Mr Fabius has emerged as a credible rival to François Hollande, the weakened Socialist leader, who has called a party congress in November. Manoeuvring among rivals is feverish. Mr Fabius's programme will be well to the left of Mr Hollande's: he promises a platform he will be proud to call socialist. "Big tax cuts will clearly not be on the agenda," said the man who, as finance minister, cut taxes.

Mr Fabius's courtship of the far left is mirrored by Mr Sarkozy's of the far right. Never one to miss a chance to play action man, Mr Sarkozy rushed to a rough housing estate near Paris after a child of north African origin was murdered. He offended liberal sensibilities by vowing to "clean out the place with a dirt-blaster". Then he said that a judge who had released on parole a man who went on to murder a young woman would have "to pay" for his mistake. Mr Sarkozy calls this the straight-talking of a man of the people, but some have detected an effort to speak to the far right. Its standard-bearer, Jean-Marie Le Pen, won 17% of the vote in the first round of the 2002 presidential election, securing himself a place in the run-off against Jacques Chirac. Mr Sarkozy has duly made security his top issue since he returned

in June to the Interior Ministry.

What explains this quest for votes at the two extremes? First, it is a response to France's shifting political landscape. Under the Fifth Republic, mainstream parties have faced opposition first on the far left, then on the far right, but not usually both at once. Today, the far-right National Front remains a force even as the hard left consolidates its place, each picking up popular voters disaffected with the centre. In 2002, 24% of working-class votes went to the National Front and 16% to the hard left.

Second, the French Socialists have never been a mass movement, unlike Britain's Labour Party. As Mr Fabius argues, the party needs broader backing if it is to break out of the 20-25% range. François Mitterrand did it by reaching out to the Communists, which ultimately took him to the Elysée in 1981. Mr Fabius makes a similar case now. “If we really think that our own allies are outdated,” he asked last weekend, “if we believe that such-and-such an anti-globalisation movement is an opponent, then who are we going to build an alliance with?”

The third element is electoral tactics. In a two-round system, a candidate needs to lean to the wings in the first round, and return to the centre to get a majority in the second. If not, genuine extremists can split the first-round vote. By sounding an authoritarian note, Mr Sarkozy hopes to rob the National Front of votes. Mr Chirac's mutterings about the “smells and noises” of immigrants when Paris mayor did not hurt his presidential chances. But such a strategy carries certain risks, and not just because it enables moderate rivals to decry distasteful politics.

One risk is that it could leave the centre ground open. Second is a problem of credibility. Will Mr Fabius, who today denounces tax cuts, appeal tomorrow to the middle classes whose tax burden is so heavy? Will Mr Sarkozy's rightward lurch alienate those in the centre whose votes he needs in a second round? In many ways, both men want to show that they embody change: something different compared with tired, out-of-touch politicians. Yet a third risk is that their attempts to do this look like the politics of opportunism, not of conviction.

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Albania's election

Berisha beacon

Jul 7th 2005 | TIRANA
From The Economist print edition

The comeback of a discredited former prime minister

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IT HAS never held a free and fair vote, so Albania's July 3rd general election came under close international scrutiny. In the event, there were few complaints of fraud, but intimidation and vote-buying were much in evidence. An official from the Republicans, a right-wing opposition party, was shot dead outside a Tirana polling station. Thousands of names were missing from the voting register compiled early this year. A mission led by the Organisation for Security and Co-operation in Europe said the election only partly complied with international standards.

Sali Berisha, leader of the centre-right Democratic Party, quickly claimed a majority in the 140-seat parliament. But 72 hours after the polls closed, the electoral commission had issued results from fewer than a third of counting centres. Albanian television gave the Democrats 55 of 100 seats contested under first-past-the-post rules, and their Republican allies at least 20 of 40 seats in a proportional ballot. But after a long period in power, including four years as prime minister, Fatos Nano, the Socialist leader, is turning out to be a poor loser. Party officials plan to contest the results in Tirana and Durres, where the Democrats made the biggest gains. The Democrats said several electoral commission staff had resigned after intimidation from Socialists. The Socialists retorted that Democrats were harassing vote-counters.

The official outcome is likely to give Mr Berisha a slim majority. But the post-election manoeuvring has not improved Albania's chances of completing a European Union stabilisation and association agreement, the first step towards eventual EU membership. Talks were postponed last year because of the Socialists' failure to tackle corruption and organised crime.

Under Mr Nano, the economy has expanded fast, driven in part by remittances from Albanians working in Italy, Greece and Britain. But unemployment is still high despite emigration. In the countryside, subsistence farming is the rule. Companies known as “monopols”, owned by prominent Socialists, have a grip on such necessities as imports of fuel and food. The failure to tackle organised crime has made Albania Europe's main warehouse for heroin, say western diplomats.

Can Mr Berisha do better? His record is not promising. He was a doctor to the late Enver Hoxha, Albania's dictator, and founded the Democratic party when Albania gave up its isolation in 1990. As president, he launched market reforms but lost credibility when he refused to shut a series of pyramid savings schemes in which an estimated 60% of the population had invested. He was kicked out of office when the scam collapsed in 1997 with losses of more than $2 billion, leading to months of anarchy in which 2,000 people died. A year later he was accused of organising violent protests to bring down Mr Nano's government. Eventually Mr Berisha apologised for tolerating the pyramid schemes, and rebuilt his party.

With the help of American consultants, Mr Berisha campaigned on an anti-corruption platform, which appealed to Albanians fed up with being asked to pay bribes and seeing jobs go to less qualified people with Socialist connections. “Corruption is so widespread it undermines society,” says Professor Gezim Karapici, of Tirana University, who ran for parliament for the Democrats as a gesture of protest. Mr Berisha may have persuaded voters he is fit to govern, but he will find it hard to put Albania back on the path to reform.

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Kosovo's future

Waiting game

Jul 7th 2005 | BELO POLJE AND GORAZDEVAC
From The Economist print edition

The Serbs in the province ponder a gloomy future

THE villagers of Belo Polje have a fine view of the town of Pec, but are too scared to go there. Before the Kosovo war of 1998-99, some 1,800 people, almost all Serbs, lived in Belo Polje. Today 40 men remain, hoping for better times. Pec is an Albanian town and the men of Belo Polje fear a lynching if they visit it.

Despite the efforts of the United Nations, the ultimate authority in Kosovo (though the place is still legally a province of Serbia), most Kosovo Serbs are cooped up in enclaves. The local ethnic-Albanian government says that the Serbs are kept in fear by their own authorities; they insist it is safe for them to travel and mingle in Albanian-majority areas. Yet a report by the UNHCR, the UN's refugee agency, says that, though there has not been an ethnically motivated murder in Kosovo for over a year, Serbs and other minorities (mostly Roma) continue to suffer attacks, harassment and intimidation. Cemeteries are vandalised and hate graffiti appear on municipal buildings.

All this is being noted by Kai Eide, a Norwegian diplomat appointed by Kofi Annan, the UN secretary-general, to report on Kosovo. If Mr Eide's report is positive, Mr Annan will appoint a “status envoy” to begin talks on the future of Kosovo this autumn. Kosovo's Albanians, who make up more than 90% of its 2m people, want independence. Serbia's leaders say they cannot have it. As Mr Eide drives around, tensions mount. Last weekend, bombs went off outside the buildings of the Kosovo government, the UN and the Organisation for Security and Co-operation in Europe; and a grenade was thrown at a building housing a branch of a Serbian political party.

Over the past few weeks, some Kosovo Serbs have been arguing for an end to what they call a self-defeating boycott of Kosovo's institutions, decreed by Serbian authorities. The government in Belgrade says that, by joining in, the Serbs would make it easier for the Albanians to say all is well, and thus that Kosovo deserves independence. There are thought to be more than 100,000 Serbs in Kosovo. The numbers displaced in Serbia range from 60,000 to 230,000, depending on whose figures you believe. According to the UNHCR, only just over 6,000 Serbs have returned home since the end of the war.

Also near Pec is the village of Gorazdevac, with some 1,000 Serb inhabitants. There is hardly any work;

to move in and out of the village, people need a twice-weekly escort of NATO-led peacekeepers. A war memorial defiantly commemorates locals killed by “Albanian terrorists” and NATO bombs. But as one local says, “if Kosovo gets its independence what would we wait for? We'd all go. There would be nothing to wait for.”

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Terrorism in Dagestan

The language of bombs

Jul 7th 2005 | MAKHACHKALA
From The Economist print edition

Islamic rebels and corruption threaten another piece of the Russian jigsaw

A MOUNTAINOUS region peopled by warriors speaking dozens of languages is never easy to run. In Dagestan, Islamic terrorists are trying to make it impossible. Dagestan seems a different country from Russia. Nearly everyone is Muslim, and public buildings are festooned with portraits of Imam Shamil, an anti-Russian leader in the 19th century. Yet Russia is what holds this republic together. Its 2.5m-strong people, comprising 34 ethnic groups, use Russian as their common language. The federal budget provides most local-government revenues. Few Dagestanis hesitate to profess loyalty to Moscow.

So why is an insurgency that aims to put in place a caliphate growing fast? The list of incidents is endless. This week a bomb blast killed two policemen, gunmen shot dead a local politician and Russian security forces said they had killed a rebel leader. Last week an explosion blew up ten soldiers outside a bath-house in Makhachkala; a few days earlier, nine policemen were wounded. A bomb derailed a train; a minister was blown up in his car; a police chief was shot on a mountain road. Most such attacks take place in or around Makhachkala, a seaside town where cattle wander across roads and drivers happily ignore the law. The only rule worth respecting, say motorists, is to keep away from police vehicles: they tend to explode.

The authorities blame the violence on Islamic revolutionaries. A group called Shariah Jamaat took responsibility for the bath-house killings. Abdulmanap Musaev, spokesman for the Interior Ministry, says foreign jihadists are recruiting locals “to destabilise Dagestan and then the rest of the north Caucasus.” Another source of trouble is Chechnya, where a decade of war, black-market weapons sales and poverty have bred extreme lawlessness. Chechen rebels, who have staged numerous forays into Dagestan, work alongside Dagestani insurgents—and vice versa.

Yet many believe that the true source of the trouble is neither mysterious “international terrorists” nor fundamentalists, but the corrupt security forces and government. The head of Dagestan's government since 1987 has been Magomedali Magomedov, a canny politician who has pleased the Kremlin by keeping a lid on local discontent. But under his rule, Dagestan has also become a prime example of a government that acts as a family business.

As President Vladimir Putin's troubleshooter in the region, Dmitry Kozak, said in a leaked report, the entire north Caucasus is largely run by “clan-corporate associations.” That explains why many in Makhachkala are surprisingly blasé about the bombings. “Serves them right,” one resident grumbles, as a patrol car passes. “Sad as it is, many ordinary people are not that concerned about the attacks on the

police, and they have a solid reason—because the police in Dagestan are not law-enforcement officers, they serve certain clans," says Isalmagomed Khabiev, chairman of an independent small-business union.

Officials insist that corruption is no worse than elsewhere in Russia, but admit it undercuts the fight against crime and terrorism. "For money, anyone can go anywhere, even abroad," one officer says. Corruption runs "right through the Interior Ministry, from top to bottom," adds another. Hatred for the government translates into sympathy for the insurgents, says Mr Khabiev. "The bombers are not really all about caliphates, but about unhappiness with the local authorities, with this criminal regime."

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Turkish corruption

Still for sale

Jul 7th 2005 | ANKARA
From The Economist print edition

Turkey's ruling party falters in its drive against corruption

ON NOVEMBER 3rd 1996, a senior Turkish police officer, a right-wing mobster and his girlfriend died in a car crash in Susurluk in western Turkey. A Kurdish deputy survived, but said he had lost his memory. The scandal exposed, as never before, the extent of the state's links to organised crime. Six years later, to the day, the Justice and Development (AK) party swept to power on pledges to wipe out corruption. Except for the Republican People's Party, not one of the sleaze-spattered parties that had ruled Turkey for the previous three decades got into parliament.

It is not human-rights abuses or Islam but graft that is the biggest obstacle to Turkey's joining the European Union and to its hopes of winning more foreign investment. The AK party government led by Recep Tayyip Erdogan has mostly done well. It prosecuted crooked businessmen and politicians (including an ex-prime minister, Mesut Yilmaz) that no previous government would have touched. It installed Hanefi Avci, a police official described as incorruptible by western peers, to head its organised-crime unit. Mr Avci won prominence when he told a parliamentary commission probing Susurluk of the army's involvement in the affair. He later tipped off the government about the generals' plans to oust it in 1997, and was demoted.

In his new job, Mr Avci sparkled anew, hauling in a string of wanted mafia dons long shielded by the establishment. But last month, just as Mr Avci was concluding an investigation into shady state energy contracts, he was ordered to the western province of Edirne, as the new police chief. Senior officials say that Mr Avci fell from grace because his probe had led him to parliamentarians from the AK party, including its secretary-general, Idris Naim Sahin, who was mentioned by name in an indictment of a Turkish company accused of cheating on a state contract to build a pipeline in north-east Turkey. Mr Avci had also upset Abdul Kadir Aksu, the interior minister, by advising him to rein in his son, Murat, a lawyer whom Mr Avci believed to be exerting pressure on investigators who were looking into a client.

Even before Mr Avci's banishment, there were signs that the AK party was not living up to its promises. It has yet to fulfil election pledges to lift legal immunity for parliamentarians, about 60 of whom face corruption charges. An anti-graft law has been shelved. Two senior AK appointees in the customs and transport ministries, who have been charged with using their position for private gain, have not been sacked. Nor has Binali Yildirim, the transport minister, who was criticised after a high-speed train accident in which 36 people died. The service was introduced even though many experts declared it unsafe.

In January, Mr Erdogan and his wife, Emine, sparked widespread controversy by accepting a $30,000 diamond necklace from a businessman (they were then obliged to return it). And this week Mr Erdogan faced fresh attacks for reversing an opposition bill that would have put Ihlas, an Islamic finance house, in the care of the state fund that reports to prosecutors on the reasons for a bankruptcy. Ihlas collapsed in 2001 after reports that its owners had siphoned off over $1 billion of depositors' funds to shore up ailing businesses in their media and industry conglomerate. “Instead of battling corruption, this government is busy covering it up,” commented Cuneyt Ulsever, a columnist on the daily *Hurriyet*.

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Charlemagne

Europe's lost leaders

Jul 7th 2005
From The Economist print edition

The last thing the European Union needs is more visionary leadership

AS THE European Union sinks deeper into political confusion and economic stagnation, a nostalgia for the good old days is setting in. Anguished Europhiles pace the Schuman district of Brussels, bemoaning the lack of a modern Schuman to chart a new future for Europe. All that is left of the great man is a giant rock bearing his name, strategically positioned outside the European Commission's Berlaymont headquarters. Schuman is not the only name that evokes fond memories. Where are today's equivalents of other figures in the Europhile hall of fame: Monnet, Adenauer, Delors, Kohl, Mitterrand? Europe's crisis, it is said in the corridors of Brussels, is above all a crisis of leadership.

It is certainly true that the European leaders who assembled at the G8 summit in Gleneagles this week make an uninspiring sight. Jacques Chirac is in deep political trouble, after his failure to persuade the French to vote yes in a referendum on the European constitution. His poll ratings are collapsing, he is looking his age and he has developed an unerring capacity for insulting fellow Europeans; having told the central Europeans to shut up a couple of years ago, this week he was overheard making sneering comments about British and Finnish food, and Britain's responsibility for mad-cow disease.

Gerhard Schröder of Germany also seems to be on the last lap of his political career. His situation is so desperate that he is committing political *hara-kiri*, by precipitating an election that he seems sure to lose. Silvio Berlusconi, the prime minister of Italy, is dogged by political and economic troubles at home—and, as always, by his own legal problems. Outside his own country, he often comes across as something of a buffoon; he started the trend for denigrating Finnish food and famously likened a German member of the European Parliament to a concentration-camp guard. José Manuel Barroso, the recently installed Portuguese head of the European Commission, who is also at Gleneagles, seems to be a man of energy and intelligence. But he has shown uncertain political judgment since he arrived in Brussels, and the commission cannot help but be tarnished by the current atmosphere of crisis within the EU.

That leaves Tony Blair as the one European leader to arrive in Gleneagles with a bounce in his step, at least before the bomb attacks in London. He has just won an election, London has been awarded the Olympics in 2012, and an accident of timing has given him the presidency of both the G8 and the EU at the same time. After a much acclaimed speech to the European Parliament, there are those (most notable, it must be said, among Mr Blair's own entourage) who see the British prime minister as well placed to give the EU the new leadership it needs. Mr Blair intends to press the case for reform at a specially convened informal EU summit in October.

Yet Mr Blair's aspirations to European leadership suffer from the fact that he too is something of a lame duck, having announced that this will be his last term as prime minister. He has been around a long time—long enough to make plenty of enemies. Few on the European left will ever forgive him for the Iraq war, and his relationship with Mr Chirac is beyond repair. Even a change of leadership in Germany and the use of the bully pulpit of the EU presidency are unlikely to be enough for Mr Blair to seize the intellectual and political leadership of Europe at this late stage of his career. Fraser Cameron of the European Policy Centre, a think-tank, speaks for many in Brussels when he argues that the EU will probably not be able to make a fresh start until the entire present generation of leaders—meaning Mr Blair, as well as Mr Chirac and Mr Schröder—has gone.

All this yearning for a new generation of decisive leaders is, however, missing the real point. Many of the problems of today's EU stem from an excess of visionary leadership, rather than a lack of it. The Kohl-Mitterrand-Delors troika of the late 1980s and early 1990s was certainly bold, and it is still revered in Brussels. But the three men's enthusiasm to create new political structures for a united Europe left them careless both of public opinion and of the need to get the economics right. The Maastricht treaty,

which led to the single European currency, was nearly tripped up in a referendum in France in 1992: a near-death experience that presaged the fiasco of this year's vote on the constitution. Similarly, Mr Kohl was notoriously uninterested in economics. For him monetary union in Europe, like German unification, was above all about politics. He assumed that the economics would work out. In fact, the mishandling of German unification has turned out to be an economic disaster for the EU as well as for Germany itself; even the economics of the euro are increasingly questioned by some of its members.

No more dreams, please

The last thing today's European Union needs is more political leadership of this sort. After the French and Dutch votes, European leaders will surely be warier of signing up to grand political visions in the hope that adverse public opinion can somehow be finessed. Of course, there are many problems facing the EU; but they are primarily economic and are better solved country-by-country, rather than by European leaders convening in a picturesque castle and spelling out some ambitious political dreams for the future.

That is partly because the legal powers to make the necessary changes to labour markets and the European social model reside above all at national, not EU, level. But it is also because the tough work of persuasion that is needed to make economic reform work can ultimately be done only by national politicians who need to convince their own voters. No EU member is going to accept the pain of reform just because Mr Blair makes a good speech in the European Parliament, or because an EU summit passes a stirring resolution. Economic reforms in France and Germany will be carried through by French and German politicians, or not at all.

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Correction: Manuel Fraga

Jul 7th 2005
From The Economist print edition

In "A farewell to Fraga" (June 25th), we incorrectly said that the Galician leader had been education minister under Franco. In fact he served only as information and tourism minister. Sorry.

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The Supreme Court

A hard seat to fill

Jul 7th 2005 | WASHINGTON, DC
From The Economist print edition

AFP

The most difficult domestic decision of George Bush's presidency

Get article background

WHOEVER George Bush chooses to replace Sandra Day O'Connor on the Supreme Court, the nomination is likely to precipitate a partisan war. Much of his second-term agenda may then be engulfed in the battle. Assuming he prevails, his choice could help put a conservative stamp upon American life that would long outlast his presidency; but he could also end up driving moderate voters away from the Republican hegemony he is striving to build.

No one in Washington, DC, has seen anything like the lobbying frenzy that greeted Justice O'Connor's announcement. From the right, Progress for America said it would spend $18m on television advertisements supporting whoever Mr Bush nominates; another conservative group, the American Centre for Law and Justice, e-mailed 850,000 people within an hour of her resignation. On the left, People for the American Way and Alliance for Justice, which between them raised $6m just for the dress rehearsal over Senate filibusters, will fight whoever the president sends for confirmation. The *Washington Post* guesses lobby groups will spend $50m-100m on this battle.

Much of the money will be squandered: it will have little impact on who gets chosen. As Tom Mann of the Brookings Institution points out, the campaigns will cancel each other out. But the war chests show how much is at stake ideologically.

For social and religious conservatives, this is the political battle of a generation, the culmination of a 25-year campaign that began with Ronald Reagan's election in 1980 and continued with the Republican takeover of Congress in 1994. The Supreme Court is the only branch of government that conservatives do not control.

For years, they argue, unelected judges have been “legislating from the bench” on issues such as abortion and gay marriage. So long as conservatives did not control the presidency or Congress, there was little they could do. But now, argues Bill Kristol, the editor of the *Weekly Standard*, they have a chance to implement a judicial revolution that will match their economic and foreign-policy achievements.

Conservatives' eagerness to seize that chance can be judged from their willingness to remove the

filibuster as a weapon in the Senate's judicial hearings and from the passions roused by the Terri Schiavo affair; in both cases frustration at the courts boiled over in congressional threats against judges. It is this pent-up passion on the right, plus the inevitable response from the left, that explains the money being spent—rather than anything that will actually change at the Supreme Court.

The judicial consequences of Justice O' Connor's retirement have been somewhat exaggerated. Ralph Neas of People for the American Way has said that if the court reflected the views of its most conservative members—Antonin Scalia and Clarence Thomas—there would be a legal revolution restricting abortion, civil rights, environmental protection and privacy. Whether that is true or not, replacing Justice O'Connor will not bring it about.

Justice O'Connor was a moderate conservative. In the 21 cases this term that ended in five-to-four decisions, she voted on 16 occasions with Messrs Scalia, Thomas and Chief Justice William Rehnquist. She has usually been with them in states' rights cases, voted with them in *Bush v Gore* and this term supported their dissent in *Kelo v City of New London* (where the court upheld local-government powers to make compulsory purchases of private property).

The main difference between her and the three harder-line conservative justices is that she tended to base her decisions on the narrow facts of a case, rather than on sweeping legal principle, leaving room to change her mind later. So if she were replaced by a doctrinaire conservative, there would be a change, but not necessarily a dramatic one.

In abortion cases, she sided with the liberals after 1992, when she voted to uphold the core principle of *Roe v Wade* (this established a constitutional right to abortion based on the right to privacy). Even without her vote, though, a five-justice majority remains in favour of the principle, so her resignation does not directly imperil *Roe v Wade*.

But it could make a difference to specific restrictions on abortion. In 2000, Justice O'Connor cast the tie-breaking vote that invalidated a Nebraska statute banning partial-birth abortions that did not allow for health exceptions if a mother's life were endangered. In its next term, the court will consider a New Hampshire law requiring minors to notify their parents if they want an abortion.

Justice O'Connor's vote was also decisive on affirmative action. In 2003, she wrote the liberal majority opinion that upheld the University of Michigan Law School's racial-preference programme, which established that diversity in education is a compelling state interest. Yet at the same time she voted with conservatives to strike down the university's admissions programme for undergraduates.

So if Justice O'Connor is replaced by a more ideological conservative, it will not change the court at a stroke. But it will change the balance of the court more than would a similar switch for the ailing, consistently conservative Mr Rehnquist (which could also happen within a year). It will make the conservative faction more doctrinaire, polarise the court further, and set the stage for a battle royal when a truly liberal justice, like the 85-year-old John Paul Stevens, finally retires.

Turn to the right

The big question for Mr Bush is how far he wants to advance the long-range ambition of social conservatives to change the court fundamentally. Although he has often insisted he has no litmus test, he has also talked about appointing a true conservative, given the chance, and offered as his models Messrs Scalia and Thomas.

The president seems to share social conservatives' dislike of “activist judges”. He has consistently nominated judicial conservatives to lower-court posts, even renominating several when the Senate failed to confirm them. And his political strategy has been founded on courting the social and religious right. For them, this is payback time. Mr Bush seems unlikely to repeat what his allies regard as one of his father's two biggest mistakes (along with raising taxes): the nomination to the Supreme Court of David Souter, a supposed moderate conservative who has turned out to be among the most liberal judges.

And yet the risks of Mr Bush heading too far to the right are huge. It would split his party. It would put abortion back on the top of the political agenda—galvanising liberals and alienating moderates. The backlash could hurt his party in the mid-term elections and the prospects for his second-term agenda, which are tarnished enough as it is. And it is not even certain this is what the president wants: if he had his way, he would probably nominate his attorney-general, Alberto Gonzales, who is unpopular with the right for being insufficiently anti-abortion.

President Reagan won plaudits for appointing the first female Supreme Court justice. Mr Bush will need the wisdom of Solomon to please even half the country in nominating her successor.

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The press and the law

Barking up the wrong tree

Jul 7th 2005 | WASHINGTON, DC
From The Economist print edition

A White House vendetta, an out-of-control special prosecutor, a lot of blather about press freedom—and the journalist who published nothing goes to jail

IT HAS been a classic showdown between the rights of a prosecutor to investigate an alleged crime and the right of the press to protect its sources. For months Patrick Fitzgerald, a federal prosecutor, has been threatening Matthew Cooper, of *Time* magazine, and Judith Miller, of the *New York Times*, with jail if they refused to co-operate with his investigation into who leaked the identity of a CIA agent.

Time eventually wilted, though only after the Supreme Court refused to hear the case. Last week, the magazine handed over Mr Cooper's notes, as well as other documents. When that failed to satisfy Mr Fitzgerald, Mr Cooper agreed to testify himself on July 6th, claiming his source had relieved him of his pledge of confidentiality. But Ms Miller refused, and was dispatched to jail. “There is still a realistic possibility that confinement might cause her to testify,” said Judge Thomas Hogan.

The case—like much else that is poisonous in Washington, DC, these days—has its roots in the Iraq war. In his state-of-the-union speech in January 2003, George Bush claimed that Saddam Hussein had tried to acquire uranium from Africa. On July 6th, Joseph Wilson, a former ambassador who had earlier gone to Niger for the CIA to investigate this, wrote an article in the *New York Times* disputing Mr Bush's assertion.

Mr Bush's people hit back. On July 14th Robert Novak, a veteran conservative columnist, published an article, sourced to two “senior administration officials”, outing Mr Wilson's wife, Valerie Plame, as a CIA “agency operative” and claiming that she had suggested to the CIA that it send her husband to Niger in the first place.

This caused a huge fuss. Mr Cooper produced a follow-up story; Ms Miller researched one, but did not publish it. Confronted with the fact that it can be a criminal offence to reveal the name of a covert CIA agent, the Bush administration decided to appoint a special prosecutor, in the form of Patrick Fitzgerald, who made his name chasing down terrorists, to find the leakers. He is still looking, if under some fairly unexpected stones.

The Plame case raises all sorts of questions. There are philosophical ones about whether journalists have special privileges that other citizens don't. There are also humdrum ones of who did what.

The most obvious question is why Mr Cooper and Ms Miller, rather than Mr Novak? Mr Novak has never appeared to be in danger of going to jail; he has never even been publicly asked to testify. But it was Mr Novak who broke the story about Ms Plame. Mr Cooper's piece didn't add anything much to Mr Novak's story. Ms Miller didn't even publish a story on the subject. It is widely assumed that Mr Novak co-operated with the federal prosecutor. But he has said little about the investigation other than that it would be “madness” to infer that he was responsible for Ms Miller or Mr Cooper going to jail.

The other obvious question is who did the leaking. Lawrence O'Donnell, a pundit at MSNBC, and Michael Isikoff, a reporter for *Newsweek*, both pointed the finger at Karl Rove, Mr Bush's powerful adviser. There is nobody liberals would rather hurt. Mr Wilson has voiced interest in seeing “whether we can get Karl frog-marched out of the White House in handcuffs”.

Yet the case against Mr Rove is far from proven. Mr Rove seems to have talked to Mr Cooper at about the time of the leak, but he talks to journalists all the time. And it was Mr Novak rather than Mr Cooper who first broke this story. Mr Rove certainly doesn't have the appearance of a man whose career hangs in the balance.

Which brings us to the more philosophical question: who is in the right in the legal stand-off? Many journalists see it as a simple issue of press freedom. The courageous Ms Miller says that “journalists simply cannot do their jobs without being able to commit to sources that they won't be identified. Such protection is critical to the free flow of information in a democracy.” But things are a little more complicated than that.

We're not that different

The first problem for journalistic purists is that, while the first amendment is absolute in its protection of the right to publish, it is far less categorical when it comes to protecting the news-gathering process. In *Branzburg v Hayes* (1972) the Supreme Court refused to acknowledge a special privilege that protects reporters from testifying in criminal cases. The US Court of Appeals for the District of Columbia has twice upheld a lower court ruling that Mr Cooper and Ms Miller should be forced to testify—and the Supreme Court has in effect endorsed that stance.

The second problem is that it is getting ever harder to argue that there is a priestly caste of journalists who possess special skills and need special privileges. The mainstream media has repeatedly embarrassed itself. The *New York Times* was caught employing a plagiarist-cum-fantasist; CBS News relied on dodgy documents to break a story about Mr Bush; *Newsweek* had to retract a story about the Koran being flushed down a lavatory at Guantánamo Bay. Meanwhile, “amateurs”, especially on the web, have run rings round professional journalists, recognising major stories before they do (as happened with Trent Lott's racist remarks) or tearing their arguments apart (as happened with CBS).

Third, confidential sources are problematic when it comes to the public interest. Journalists have a *private* interest in cultivating confidential sources to maximise their access to privileged information. But was Mr Novak's original story serving his readers or his private source? Ms Miller's sources helped produce a series of scoops during the run-up to the Iraq war about Saddam's weapons of mass destruction. But the *New York Times'*s public editor later conceded that the paper's coverage of Iraq had often consisted of “breathless stories built on unsubstantiated revelations that, in many instances, are the anonymity-cloaked assertions of people with vested interests.”

You can certainly argue that, in the long term, the complicated dance between confidential sources and journalists helps the free flow of information. Mark Felt, the now revealed Deep Throat, was clearly acting out of private grievance as much as a sense of the public good. But you can also see why courts see no automatic connection between protecting free speech and protecting anonymous sources.

The journalists are not the only people on slippery ground. Mr Fitzgerald looks ever more like a run-away special prosecutor. He has not only allowed a case about a leak to morph into a case about press freedom (“Journalists are not entitled to promise complete confidentiality”, he recently asserted. “No one in America is.”). He has also gone after Mr Cooper and Ms Miller with a determination and ferocity that is completely out of proportion to their alleged misdemeanours. It is possible that, in an odd replay of the Monica drama, he may now be primarily trying to prove that somebody in the White House has perjured himself or herself.

One problem for Mr Fitzgerald may well be proving that Mr Novak's sources broke the law in the first place. The Intelligence Identities Protection Act of 1982 includes all sorts of stipulations and categories. In one category, the leaker must have authorised access to classified information; he must reveal the agent's identity intentionally; the government must be taking “affirmative measures” to conceal the agent. In another category, the leaker must be engaged in a pattern of behaviour intended to harm national security.

These caveats are hardly surprising. The statute was intended to prevent the treasonous betrayal of secret agents in the field, rather than the cheap vendettas of White House operatives. Mr Fitzgerald has spent an unusual amount of public money following up on Mr Novak's column; and now one person who never published anything is in jail. Let's hope that, when it comes to the real question—whether anybody in the White House broke the law—this doesn't all turn out to be much ado about nothing.

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Prisons

Jailhouse vote

Jul 7th 2005
From The Economist print edition

Iowa will now let former prisoners vote

IT WILL “symbolise Independence Day, of sorts”. That was how Governor Tom Vilsack explained his generous decision on July 4th to give all Iowa's ex-prisoners a vote. Previously, any felon released from the state's prisons had to go through an application process of between three and six months to get his vote back. Around 50,000 Iowans who either didn't bother or were denied their appeal can now vote again.

Virtually every American state puts some limit on former prisoners voting, including waiting periods after release and restrictions on prisoners on parole. A handful automatically restrict voting rights for all prison-leavers. Iowa joins its neighbour Nebraska, which removed restrictions earlier this year, in giving votes back to all.

The current system is unfair to prisoners trying to rejoin society. It is also strongly biased against Democrats such as Mr Vilsack (who, incidentally, is stepping down soon, and is sometimes mentioned as a potential candidate for the Democratic presidential nomination). Chris Uggen, a sociologist at the University of Minnesota, has modelled how former prisoners might vote. He says that “at least seven in ten former felons would prefer a Democratic candidate”. That would have changed the result of at least seven Senate races over the past 16 years and “swung Florida to Al Gore by a 60,000-vote margin” in the controversial 2000 election.

Florida, as it happens, is the main focus of those who would like to see the system changed. According to The Sentencing Project, a lobby group, half a million Floridian ex-felons currently have no vote. Most of those who want to get it back have their appeals heard at a quarterly public meeting, presided over by Governor Jeb Bush and a panel of three officials. The hearings deal with no more than 500 prisoners a year, which sounds fine; but as Florida's Parole Commission has a backlog of 8,855 appeals, it can take years to get voting rights back. Many ex-felons don't bother.

The problem is compounded because many Florida state jobs can go only to people who are allowed to vote. Disenfranchised former prisoners can be denied work in an eccentric range of jobs, from athletic trainer to funeral director.

Despite these oddities, Jeb Bush is not in favour of change. His brother, however, seems to take a different view. “America”, the president has said, “is the land of second chance, and when the gates of the prison open, the path ahead should lead to a better life.” So it should.

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The National Guard and reserves

Once was enough

Jul 7th 2005 | BAGHDAD AND TIKRIT
From The Economist print edition

Many reservists have already been to Iraq; soon they will probably have to go back

Get article background

"DONALD RUMSFELD'S bitten off more than he can chew in Iraq—and my ass is a piece of that." That is the opinion of one American chief petty officer in Baghdad on the controversial planning of the defence secretary. A veteran of 14 years' active duty, the officer left the navy two years ago, only to be coaxed into the reserve by his former commanding officer to fill a job in Iraq. This was unfair pressure, he now feels: "I gotta job, a wife, kids. I do not want to be in Iraq."

Few reservists in Iraq would pity him. He knew he was bound for Iraq when he signed up for the reserve; most did not. In addition to its 1.4m active-duty forces, America has called heavily on the 1.2m part-timers (though they hate that term) gathered in its regular reserve forces and the National Guard. The former comprises part-time soldiers, many of them veterans and technicians (including doctors). Each state also has a National Guard force, technically under the control of the governor, but answerable to the president.

So far, Mr Rumsfeld has used some 500,000 reservists of various sorts in Iraq and elsewhere. The two biggest contributors have been the army guard (which musters 332,000) and the army reserve (around 200,000). Currently they account for virtually all the 41,000 reservists in Iraq—or around 30% of the total American force there. This percentage has fallen from around 50% earlier this year, as the stock of ready reserves has been exhausted.

The army reserve is used to being called overseas to supplement active-duty troops. For the army guard, the burden has been more unusual. These "weekend warriors" have seldom been employed overseas, except in time of war—and Iraq's predicament is not technically that. Many guard recruits were drawn in by help with university fees, in exchange for 12 weekends and two weeks of training each year.

For the better connected—including George Bush and Dan Quayle—the National Guard used to be a virtuous way to avoid fighting overseas. But since the draft was abolished in 1973, its units have increasingly been trained, equipped and deployed in-line with active-duty units. Three days after the September 11th attacks, Mr Bush authorised the call-up of 1m part-timers, for up to 24 months. Roughly two in three guards have since been deployed somewhere—to secure America's borders, to Afghanistan or to Iraq. "9/11 changed the perception entirely," argues Major-General Joseph Taluto, who now heads the first guard division to be deployed overseas since the Korean war; it is in Tikrit.

A chat with the general's men suggests he is right. Sergeant Gary Sundgren, a veteran of 18 years' service, whose only previous deployment was to clear space-shuttle wreckage, says few guard recruits expected to be deployed overseas. "But no one twisted our arms, no one drafted us," he admits. His view is echoed across his company. None seems happy to be in Iraq—for one year, after six months' special training. Several say recruiters promised they would not be deployed; several worry about the studies they had to postpone. But none is very unhappy either. The company's recent triumph in intercepting a suicide car-bomber is a greater preoccupation.

America's presence in Iraq has depended on the forbearance of such men. Despite the billowing insurgency, Mr Rumsfeld has sneered at demands to recruit more regular troops. In fact, even to sustain the current troop numbers in Iraq, America's part-timers will soon have to see more than the currently stipulated 24 months of service.

This is worrying, because recruitment is already flagging. From October to April, the army reserve

recruited 73% of its target number; the army guard recruited 77%. More recent figures are not expected to be healthier, despite extra inducements such as a guard re-enlistment bonus of $15,000. In March, the age limit for all reservist recruits was raised by five years, to 39.

To forestall the inevitable recycling of reserves, Mr Rumsfeld is working the regular forces hard. Many are on active deployment half the time. But the regulars are missing their recruitment targets too. If America is to maintain its current commitment in Iraq for two years—as senior officers say it must—more “part-timers” will have to return there.

There are possible schemes to ease the pain. The guard and reservists could be put into units deployed for shorter periods, or be bribed to volunteer for lengthier deployments. But in the longer term America's armed forces face a serious problem. Iraq is only one of the jobs they are meant to be doing. They also have to defend the homeland, deter conflict in the Koreas and, potentially, according to the current military doctrine, fight another war.

Mr Rumsfeld's resistance to recruiting a much bigger regular army stems in part from his dogmatic adherence to high-tech fighting. But in light of the recent recruitment figures, it is hard to see where these fresh warriors would come from anyway. Andrew Krepinevich, of the Centre for Strategic and Budgetary Assessments, puts it this way: “It is ironic that America today is sometimes compared to the Roman Empire: its people, like the Romans two millennia ago, seem increasingly reluctant to fight for their security.”

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Minnesota's budget

Divided we fall

Jul 7th 2005 | ST PAUL
From The Economist print edition

The politics of polarisation arrive in a friendly state

AP

Bad time to renew your driving licence

ONCE it was known as “the state that works”. But Minnesota has now joined Tennessee as only the second state for a decade to face a shutdown. Because its politicians failed to agree on a two-year budget by the statutory deadline, July 1st, 9,000 state employees are now out of work. State health-care programmes are still running, and parks were kept open for the July 4th holiday, but “non-essential” services—such as renewing driving licences—have been suspended.

Voters are furious, but the shutdown is a cathartic moment after several years of malevolent political torpor. The ostensible reason for the breakdown is split government. Democrats, who used to regard this traditionally liberal state as their bailiwick, remain narrowly in charge in the Senate, but Minnesota now has a Republican governor, Tim Pawlenty, and a small Republican majority in the House.

In fact, both parties have shunned compromise for quite some time. This is partly a matter of ideology. The right, on the ascendant, won't give way on the need to roll back entitlements; the left, on the defensive, won't give up the last bits of the state's trademark high-tax, high-service approach. And this split has a personal edge. In keeping with its Scandinavian heritage, Minnesota used to be a friendly place to be a politician. Now legislators from different parties barely talk to each other.

The current crisis (and the grudges) date back to 1999 when, at the eleventh hour, the tripartite government (which then included an independent governor, Jesse Ventura) agreed on an unwieldy compromise budget. Four years later, a two-year deficit of more than $4.2 billion was “solved”, again partly by more accounting gimmicks, but also by a shift to the right: there were cuts to state health-care programmes, a tiny increase in education spending and no new taxes. In 2004, the Democrats struck back, preventing passage of a crucial state-bonds bill. Weirdly, voters punished the Republicans: 13 House members were ousted in that year's elections, slashing their majority and emboldening the Democrats.

This year was meant to be different. Legislators attended pre-session seminars on political compromise, and the leaders promised collaboration. But it all went sour when the time arrived to deal with education and health care (which together account for more than two-thirds of all state spending). Faced with a biennial deficit of close to $800m in a total budget of $30 billion, Republicans demanded cutbacks and reform. But Democrats wanted more money for both education and health care; the cash, they said,

could come from a cigarette tax, which is popular, and a new income-tax bracket for the state's wealthiest, which is not.

Since then, Governor Pawlenty has been in obvious discomfort. Together with the House speaker, Steve Sviggum, he agreed to small increases in spending on health and education, claiming that the gap could be closed by accounting shifts and gambling revenues, but this tolerance of vice only irritated social conservatives.

At first, Mr Pawlenty stuck to his pledge not to raise taxes. Then he agreed to a 75-cent levy on each packet of cigarettes, calling it a “fee”. Such semantics did not prevent anti-tax groups from running ads against him. Nor did it appease the ungrateful Democrats. As the deadline approached, it still seemed likely that a last-minute compromise could be hacked out. Instead, the Democratic Senate majority leader, Dean Johnson, adjourned the special session, claiming the Republicans had backtracked.

After the shutdown, the furious governor began the process again. As *The Economist* went to press, the two sides were trading offers, the bitterness complicated by the fact that nobody is really sure who is gaining from the stand-off.

It may be that neither side is. Many Minnesotans may simply vote against any incumbent in the next election, argues Craig Grau, a political-science professor at the University of Minnesota-Duluth. If so, the shutdown might once again advance the cause of third parties (of which Minnesota has a rich history), though none looks exactly well organised at the moment.

As for the Democrats and Republicans, some optimists claim the cathartic shock will persuade both sides to stop pandering to their bases and find ways to solve the state's problems. Getting to know each other would be a start.

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Lexington

The right's Little Big Horn

Jul 7th 2005
From The Economist print edition

A scandal over Indian gambling threatens the conservative establishment

IN 1994, just as Newt Gingrich's Republicans were storming Capitol Hill, Christopher Buckley published his satirical novel “Thank You for Smoking”. It featured an informal lunch club of Washington lobbyists, consisting of the chief spokesmen for three of the most despised pressure groups in the country—the Society for the Advancement of Firearms and Effective Training of Youth (SAFETY), the Moderation Council (formerly the National Association for Alcoholic Beverages), and the Academy of Tobacco Studies. The club happily marches under the name of “the Mod Squad”, or the Merchants of Death.

The Mod Squad's antics look humdrum compared with the alleged antics of two of today's most famous influence-peddlers: Jack Abramoff and his side-kick, Michael Scanlon. They are not only accused of bilking six Indian tribes out of some $66m, but of using the religious right to do it.

It should be stressed that despite congressional committees and a federal grand jury looking into their affairs, Messrs Abramoff and Scanlon insist they have behaved ethically. They have not been charged with any offences. Nevertheless, according to their accusers, the story allegedly goes like this.

Mr Abramoff was hired to protect various Indian tribes from sundry threats to their gambling interests—particularly the threat of competition from rival tribes. He then got prominent social conservatives to oppose the creation of rival casinos, ostensibly in the cause of protecting public morality. In 1999-2002, Abramoff-linked organisations paid around $4m to a company run by Ralph Reed, the former head of the Christian Coalition, in order to organise a grass-roots campaign against a Texas tribe that wanted to compete with Mr Abramoff's clients, the Coushatta tribe in Louisiana. With amazing chutzpah, “Casino Jack” then turned to the defeated Texans and offered to champion their cause—for a fee.

According to Mr Abramoff's accusers, the sheer success of his caper forced him to bend even more rules. He skirted the lobbying industry's disclosure laws by getting the tribes to make most of their payments to Mr Scanlon, who was a public-relations specialist rather than a registered lobbyist. He persuaded the tribes to make generous contributions to leading congressmen and conservative groups. And he established a collection of front organisations such as the American International Centre—a think-tank in the business of influencing “global paradigms in an increasingly complex world” and bringing “great

minds together from all over the globe", which was housed a couple of blocks from the sea in Rehoboth Beach and employed as its two directors David Grosh, Rehoboth's "lifeguard of the year" in 1995, and Brian Mann, a former yoga instructor.

The Abramoff scandal has everything you could want from an inside-the-Beltway blockbuster. It has hypocrisy. What was Mr Abramoff, a vigorous defender of traditional values, doing with gambling houses? Mr Reed has not been accused of doing anything dishonest, but Christian conservatives in Georgia, where he is running for lieutenant-governor, may ask him how he squares his association with Mr Abramoff with his previous claim that gambling is a "cancer on the American body politic". It has racism. Mr Abramoff allegedly called his clients "monkeys", "morons" and "troglodytes". And, above all, it has the potential to shake the Republican establishment to its foundations.

Investigating Messrs Abramoff and Scanlon is one of Washington's growth industries. The Senate Committee on Indian Affairs, headed by John McCain, is examining their treatment of Indians. The Senate Finance Committee is investigating their use of non-profit organisations. The executive branch has put together a task force that draws from the Interior Department, the IRS, the National Indian Gaming Commission and the Justice Department. The FBI reputedly has 30 agents on the case.

Mr Abramoff has been at the centre of the conservative movement for 25 years. His pals include not just Mr Reed but Grover Norquist, the king of the anti-tax movement (and the executive director of the College Republicans when Mr Abramoff was national chairman), and Tom DeLay, the troubled majority leader in the House. Mr Abramoff helped to arrange some of Mr DeLay's controversial foreign junkets. Mr Scanlon used to work for Mr DeLay.

Under scrutiny

Two things seem clear. First, the Republican revolutionaries who promised to purify Washington back in 1994 have changed the capital less than it has changed them. Many of Newt Gingrich's radicals are now making a good living exploiting the very government that they once despised. George Bush's presidency has seen the fraternity of lobbyists doubling in size, from 16,342 in 2000 to 34,785 today.

Second, the deepening association between Indians, gambling and politicians guarantees trouble. At a recent meeting of the Senate Committee on Indian Affairs, everybody was full of sympathy for Mr Abramoff's Indian clients. But many of them are well heeled, thanks to those casinos. And they hired Mr Abramoff to use the might of the government to crush the competition. The 1988 federal law that authorised casino gambling on Indian reservations was dependent on state laws. That created a sharp divide between winners and losers: only two-thirds of America's 350 Indian tribes may tap into an industry with revenues of $15 billion a year. It also ensured that the tribes are permanently entangled with politics.

Even if he were eventually to take a tumble, Casino Jack may yet be able to reinvent himself. He has other strings to his bow, including restaurants, movie production ("Red Scorpion", starring Dolph Lundgren) and a long record of charitable work. What happens to the conservative movement is harder to say.

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Mexico

Money, the machine and the man

Jul 7th 2005 | ATLACOMULCO
From The Economist print edition

AP

A key state election shows how Mexico's formerly ruling party could seize back the presidency next year

Get article background

SAY something often enough, and it may come true. So it was in this week's election for governor of the state of Mexico. Posters proclaiming Enrique Peña Nieto “Your governor 2005-2011” blanketed the state and Mexico City, which it surrounds on three sides. Mr Peña, the candidate of the Institutional Revolutionary Party (PRI), which ruled Mexico for seven decades until its defeat by Vicente Fox in 2000, duly won the election on July 3rd with almost half the vote.

The election in the state of Mexico, with a population of 15m, is not only the largest sub-national contest but the last important state vote before the presidential election in July 2006. So it was closely watched for pointers to Mexico's political future.

In the event, it delivered two clear lessons—and several uncertainties. First, support for Mr Fox's conservative National Action Party (PAN) is plunging. In a state which he might once have hoped to win, the PAN's Rubén Mendoza gained only 26% of the vote, barely ahead of Yeidckol Polevnsky of the left-wing Party of the Democratic Revolution (PRD). In Nayarit, a small western state whose governorship was narrowly won by the PRI on the same day, the PAN took just 6% of the vote. All this suggests that the presidency lies between the PRI and Andrés Manuel López Obrador, the PRD mayor of Mexico City.

The second lesson is that the PRI's spending power and machine—both stronger than those of the PRD—can bring victory. As well as his posters, Mr Peña spent at least $14m on television and radio advertisements. The money backed a persuasive candidate. Aged only 38, with the charm of a young Bill Clinton, Mr Peña has a popular touch. At a campaign rally in Atlacomulco, his hometown, he waded to the podium through an adoring crowd of women, who cheered his promises of hospitals and highways. A despairing Mr Mendoza responded with the slogan, “I'm ugly, but I know how to govern.”

The campaign's central issue became whether the PRI's spending broke a legal limit of $20m—and if it did, whether the electoral authority will do anything about this. PRI officials dismissed the criticisms as an attempt by losers to disqualify a winner. The PAN had accused the PRI of spending more than $40m, but conceded defeat. Not so Ms Polevnsky: she called the result illegitimate and called for a re-run.

Such arguments are reminiscent of the bad old days of one-party rule. Mexicans had hoped that the establishment in 1996 of the Federal Electoral Institute (IFE), an independent body, and its equivalents in the states, had put the integrity of elections beyond dispute. Yet in the state of Mexico, the local electoral commission was rocked by scandal in May. All its members resigned when they were found to have taken bribes on a contract to print the ballot slips. José Núñez, the commission's new head, says that he has no way of knowing how much the PRI spent, partly because of deep discounts offered by Mexico's two main television companies. He says it will take two years to complete an investigation into campaign spending; he admits that while the commission could in theory ban an offending party from the next election, in practice this has never happened. Even Mr Peña concedes that the system is flawed. “Campaigns should be shorter and cheaper,” he says.

The PRI was helped in the state of Mexico by a record low turnout (42%), making the power of its get-out-the-vote machine decisive. Turnout in the presidential election is likely to be higher. The PRI faces other disadvantages in relation to Mr López Obrador, long the front-runner in the polls. While he is unopposed within his party, the PRI has not quite anointed its candidate; it may hold a primary later this year. The chosen one is likely to be Roberto Madrazo, the PRI's president. But he faces a challenge from Arturo Montiel, who as the outgoing governor of the state of Mexico will get a temporary boost from Mr Peña's triumph. The state election suggested that Mr López Obrador had no coat-tails. But according to Daniel Lund of Mund Americas, a pollster, polls showed that many of those who did not vote for Ms Polevnsky will vote for Mr López Obrador.

The most worrying signal from the state of Mexico is the new fragility of the electoral authorities. The IFE played a crucial role in 2000 in assuring Mexico's first-ever free and fair presidential election. But the IFE's new board is less respected and more partisan than its predecessor. Whatever the eventual outcome of next year's election, the state of Mexico may have provided a pointer to the following one. However much he spent, Mr Peña looks like a politician with a future.

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Brazil's bribery scandal

From bad to worse

Jul 7th 2005 | SÃO PAULO
From The Economist print edition

Heads roll in the Workers' Party

AS BRAZIL'S political bribery scandal moves from allegation to evidence, it is starting to topple leading figures in the governing Workers' Party (PT) and has forced Luiz Inácio Lula da Silva to reshuffle his cabinet to try to shore up his presidency. This week the PT's treasurer, Delúbio Soares, and its secretary-general, Silvio Pereira, took “leave of absence” from their jobs. The PT's president, José Genoino, a leading party moderate, may be next. Speculation is stirring that Lula himself will not run for re-election in 2006.

The PT's troubles began last month when Roberto Jefferson, a disgruntled government ally, alleged that party officials bribed congressmen from two parties which are part of Lula's coalition to vote for government bills. Those claims are denied, but each week's revelations seem to offer at least circumstantial support for the charges. Mr Jefferson named Marcos Valério de Souza, the owner of two advertising agencies with large contracts with state companies, as the intermediary between the PT and congressmen who accepted a monthly stipend, dubbed the *mensalão,* of 30,000 *reais* ($12,765). It transpires that Mr de Souza's agencies withdrew large sums from banks at times and places where politicians suspected of taking the bribes (or their aides) were also present.

More devastating is evidence that Mr de Souza acted as financier to the PT. *Veja*, a weekly magazine, published documents showing that he had guaranteed a bank loan of 2.4m *reais* ($1m) to the PT and even repaid an instalment of 350,000 *reais*. With his signature on the loan document were those of Mr Soares and Mr Genoino, who insists he barely knew Mr de Souza.

The suspicion is that the PT used Mr de Souza to milk public companies in order to fill its own coffers as well as to bribe allied congressmen. A leader of the Brazilian Democracy Movement Party (PMDB), a government ally, has said that Mr de Souza was part of an inner group that “exercised political and administrative influence in the government.” Brazilians are stunned: the PT, a party that claimed to hold a copyright on clean government, is mixed up in a veritable Kama Sutra of corruption.

The government hopes to steady itself by giving a bigger role to the PMDB, a large and amorphous centrist outfit. On July 6th, before flying off to the G8 summit in Scotland, Lula gave the energy and health ministries, both previously held by the PT, to the PMDB. Further changes are to follow on the president's return. The reshuffle's main value probably lies in showing that Lula is trying to clean up his administration, since the PMDB remains split between pro- and anti-government wings.

Mr da Silva does not seem tempted to resort to economic populism, which would anyway risk angering voters who value low inflation as much as faster economic growth. But the PT's moderate wing, to which Lula belongs, risks losing control of the party in internal elections due in September. Unless the allegations touch Lula personally, he could still recover. So far they have damaged the image of the PT more than that of the president or his government. The economy may well be growing strongly again next year. Brazilians may yet forgive Lula for the *mensalão*. They are unlikely to forget it.

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The Caribbean

Murder and the media mob

Jul 7th 2005
From The Economist print edition

A tragedy in Aruba brings an invasion

AP

ALL suspected murders are appalling tragedies for the families of the victims, but only a few become media circuses. To qualify, it helps if the victim is young, white, female and beautiful. That is the case with Natalee Holloway, an 18-year-old who vanished on May 30th on the last night of a high-school trip to the Caribbean island of Aruba. Spurred by Ms Holloway's battling mother, FBI investigators, private search teams and five American television crews have taken up residence on the island.

Aruban police held three young suspects for questioning (two have been released); briefly held, too, was the father of one of them, who is a judicial official. That prompted stories of an official cover-up. American radio stations have threatened a tourist boycott. That might devastate the island: it depends on tourists, three-quarters of whom (530,000 last year) are Americans.

What has been lost in much of the media storm is that Aruba, a self-governing unit of the Netherlands, may have something of a drug problem but is generally safe, prosperous and well-governed. In fact, it is much safer than the United States. In proportionate terms, it has less than half as many murders—and all seven cases since the start of 2003 have been solved. The American State Department reported in March that Aruba's judiciary “has a well-deserved reputation for integrity”.

On July 3rd, a 15-year-old blonde American was stabbed by her local boyfriend in an idyllic fishing village on Tobago, another Caribbean island. The case attracted less attention, perhaps because it lacked the terrible suspense of Ms Holloway's disappearance. The murder of two young black men from New York in the United States Virgin Islands on June 15th was barely noticed. Still less are the problems of Jamaica, which had 1,445 murders last year and whose gang wars spill over to New York.

Assuming Ms Holloway is indeed dead, it is to be hoped that Aruba can bring her killer(s) to justice. And the threatened boycott? Memories are short, and there are risks everywhere. Americans are unlikely to stay away.

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Peru

Blooming desert

Jul 7th 2005 | ICA
From The Economist print edition

An agricultural revolution

AS HE drives along the Pan-American Highway near Ica, a city four hours south of Lima, Elmer López has to use both hands to point out the farms on either side of the road who are his customers. Mr López, an agronomist, advises a rapidly growing number of paprika farmers. A few years ago, the mild pepper was scarcely produced at all in the country. Now it is the new darling of Peruvian farming, with exports of $50m last year, up from just $6m in 2000. This year, the figure will reach $80m, reckons Mr López.

Paprika is the latest recruit to a revolution in Peruvian farming. Over the past 15 years, the country has added almost 400 different export crops to its traditional staples of coffee, cotton and sugar. Farmland has increased from 1.7m hectares (4.2m acres) in 1993 to 2.6m today, according to the national statistics institute. Farm exports totalled $1.1 billion in 2004, up a third on the previous year. In the first four months of this year, they rose by another 28% over the same period last year. In the Ica area, export agro-industry has created some 40,000 jobs in the past decade.

This growth holds out the hope that Peru can repeat Chile's development path of the past two decades. Whereas in Chile, wine, salmon and fruit are the stars, Peru's champion products are vegetables and tropical fruit. First came asparagus. It began to be grown in Ica a dozen or so years ago; last year, exports of asparagus were worth $235m. Artichokes, olives, citrus fruits, mangoes, avocados and grapes have followed. All these crops are grown in Peru's coastal desert, whose stable temperatures and (so far) adequate underground aquifers for irrigation allow year-round production.

Until recently, what had held farming back was poor government policy. In the 1970s, a military government expropriated all big estates and commercial farms, turning them over to co-operatives. Almost all the co-operatives have now been broken up into individual plots, while commercial farmers have set up on previously barren land in the desert. Two decades ago, for example, the Villacurí plain outside Ica was a rolling moonscape of sand; today, it is home to 6,000 hectares of export crops.

The other factor allowing Peru's farm export boom was the decision by the European Union (EU) and United States to eliminate tariffs on thousands of products from the Andean countries, so as to encourage alternative crops to illegal drugs. The EU recently renewed duty-free access. The United States' Andean Trade Promotion and Drug Eradication Act expires in December 2006. Peru, along with Colombia and Ecuador, is holding talks with the United States over a free-trade agreement. But it is unclear whether this will be approved by the United States Congress. Asparagus growers fret that without it they will go back to facing a 21% tariff.

While export farmers on the coast are gung-ho for free-trade, their traditional peers in the Andes worry that they will not be able to compete with subsidised American agribusiness. On July 4th, groups of these farmers began a protest against the free-trade talks. This attracted little support. Provided that worries about market access and water supplies prove to be unfounded, Peru's farming revolution could still have a long way to go.

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Venezuela's armed forces

Paymaster general

Jul 7th 2005 | CARACAS
From The Economist print edition

The price of peace in the barracks

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Reuters

Driving for the revolution

ALTHOUGH he was democratically elected as Venezuela's president, Hugo Chávez is a former army officer and often says he heads a "civilian-military" regime. Many officers have senior government jobs. In this and other ways, the armed forces are the mainstay of his "Bolivarian revolution", named after South America's independence hero, which lacks a strong political party. His opponents dream that it will be the army which eventually topples the president, as it almost did in 2002. Loyalists retort that they can dream on. Certainly, the evidence suggests that Mr Chávez now has a tighter grip over the armed forces—but at a price.

The constitution drawn up under Mr Chávez gives the president sole authority over promotions. He has used this to purge the more talkative dissidents. On July 4th, he appointed a close ally from the navy, Orlando Maniglia, as defence minister.

But murmuring in the ranks may not have entirely ceased. A military ceremony on June 24th was cancelled for fear of an assassination attempt against Mr Chávez. At a scaled-down version, held at Fort Tiuna, a massive military complex in Caracas, the president called for "unity, unity, unity". He also announced pay rises of 50-60% for the armed forces. To some, that looked like an attempt to buy military loyalty; it sparked protests from civilian public employees, whose increase was less than half that.

Mr Chávez is also providing more kit. The United States and Colombia have questioned Venezuela's recent arms purchases from Russia, including 100,000 Kalashnikov rifles and a dozen or so helicopters, due to begin arriving soon. But it is hard to argue that these are offensive weapons, or that they disrupt the regional military balance.

One potential source of disharmony is the national guard. Though treated as the army's poor relation, it is 23,000-strong and has some heavy weaponry. It was once a hotbed of opposition to Mr Chávez. The government recently abolished one of its regional commands, citing corruption, and turned over its responsibilities to the army. Officials felt obliged to deny any plan to disband the guard. Another possible cause of military discontent is Mr Chávez's close ties with Cuba. Fidel Castro was recently named as the patron of a graduating class of officers—some say in a bid to flush out dissidents.

Mr Chávez is shaking up the country's military doctrine and the role of the armed forces. He has repeatedly claimed that the United States has plans to assassinate him, and even to invade Venezuela to grab its oil deposits. He is setting up a new force of reserves, which he claims will eventually comprise up to 2m members.

In practice, the reserve will be a popular militia under Mr Chávez's direct command. Its main job may be to defend the Bolivarian revolution against its internal opponents. Whatever the revolution's denouement, Mr Chávez's lasting legacy will include politicised armed forces. The revolution, as the president has often declared, may be peaceful—but it is armed.

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Development and governance

Africa acknowledges it must help itself

Jul 7th 2005
From The Economist print edition

In return for a lot more aid, Africa has promised to monitor itself a lot more rigorously. That new resolve is already being tested

WHILE the leaders of eight of the world's richest countries gathered this week at Gleneagles in Scotland, their African counterparts, who run most of the world's poorest countries, gathered at the coastal town of Sirte, in Libya, for their own jamboree under the aegis of the African Union (AU). Despite a vast gulf in media coverage of the two meetings, they were, in fact, tightly linked. For in the new mood of scaling up aid to the poorest countries, Africa's own institutions, with the AU to the fore, are now being expected by rich countries to shoulder more of the burden for curing the continent's ills.

In the next few weeks the revamped AU, together with its much-vaunted offshoot, the New Partnership for Africa's Development, better known as Nepad, will face their first big tests of credibility. If these two bodies prove as feeble as their predecessors, the current wave of Afro-optimism in western capitals may fast turn to cynicism, as it has done before. Indeed, some fear that the AU, in particular, has already fallen down on its job.

The AU, which was a relaunch in 2002 of the decrepit old Organisation of African Unity (OAU), and Nepad were both created out of a fresh resolve by African leaders to “own” more of Africa's problems themselves rather than rely on the usual alphabet soup of international agencies and NGOs to feed their starving and stop the continent's civil wars. Nepad was set up in 2001 as the economic development arm of the OAU (and then of the AU), made up of all 53 of Africa's countries. This new spirit of African ownership matches the latest trend in the development world, whereby donor countries and multilateral organisations devolve as much responsibility as possible for anti-poverty and health programmes to the recipient countries themselves, rather than micro-manage them as in the past.

So documents like the recent report of the Commission for Africa, set up last year by Britain's Tony Blair to “take a fresh look at Africa” and how to develop it, burst with enthusiasm for the AU and Nepad. In turn, these two bodies have explicitly promised to uphold human rights and democracy, to fight corruption and promote good governance. And both outfits promise to hold their members to account, to prod them to meet these stringent criteria.

The most explicit mechanism for doing so is Nepad's African Peer Review Mechanism (APRM). The 23 countries who have so far joined this voluntary scheme all offer themselves up for scrutiny by a panel of outside experts. Confidential reports are then handed to the subject governments, and a programme of

action for improvements in such things as transparency and democratic accountability is agreed on and made public. At least, that is the plan. Last week, the experts handed their verdicts to the first two guinea pigs, Ghana and Rwanda; final reports and action plans are due out next month.

The implicit deal with rich countries is that if the AU and Nepad can start to enforce western standards of financial transparency and democracy in African countries, then more aid will flow their way to foster the good work. An early example of this hoped-for new trust between the West and Africa was last year's decision by NATO countries to lend the AU logistical help to move African soldiers around the vast area of Darfur, Sudan's troubled western province, as part of a drive to encourage Africa to run its own peacemaking and peacekeeping show.

Cheerleaders for the AU point to other, arguably more successful, interventions. The AU's robust refusal this year to endorse a coup in Togo, after President Gnassingbé Eyadéma died (and his son tried to take over), led to an election, though its fairness was disputed—and it resulted in the same son becoming president. The AU has also been trying hard to broker a peace between northerners and southerners in embattled Côte d'Ivoire.

But the AU and Nepad have a pack of sceptics on their heels. The AU, they say, has already clattered into its first serious hurdle: Zimbabwe. AU observers were mealy-mouthed about the flawed election there in March, and the organisation has refused to condemn, let alone try to stop, President Robert Mugabe's recent urban clearances which have left about 300,000 homeless. Mr Mugabe remains a hero for many Africans; but the AU, by its refusal to say or do anything about his flagrant abuse of human rights, has let itself down.

Equally, it has had nothing to say about the post-electoral clampdown in Ethiopia, where it is based. This has perplexed some of the AU'S staunchest supporters. Demonstrators have been shot dead, opposition leaders detained and the election result postponed. Wiseman Nkuhlu, who heads Nepad's secretariat, says “there is no justification for that kind of thing and the AU must deal with the Ethiopian situation.” An impression is gathering that the AU is happy to take on smaller or more clear-cut cases, like Darfur or Togo, but baulks at more complex and demanding ones, such as Zimbabwe and Ethiopia.

Likewise with peer review. Moeletsi Mbeki, a businessman and brother of South Africa's president, Thabo Mbeki, argues that it is nothing more than a “sop to donors”. Sceptics doubt whether the upcoming reports on Ghana and Rwanda, the two first countries to face scrutiny, will be rigorous enough.

If the AU and the APRM are to disprove the doubters, now is the moment. Kenya, a byword for corruption again, is the next country to face its peers; a report is due out in a few months. If rigorous and detailed, it would go a long way to showing that African governments can be trusted to police themselves. In the same spirit, critics are waiting for the AU to uphold its own professed principles on democracy and human rights in countries like Zimbabwe and Ethiopia. Otherwise it and Nepad will be rightly condemned as the same useless talking-shops of the bad old days. And that would once again erode the willingness of the latest generation of western donors to pay more for an Africa that shrinks from taking the tough measures needed to put its house in order.

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Congo

Democracy postponed

Jul 7th 2005 | KINSHASA
From The Economist print edition

Worries are growing as Congo's election timetable slips

Reuters

Only 28m more needed

THE date came and went—and there were no elections, just more violence. June 30th was the original deadline for Congo's provisional government to hold the first nationwide elections since the end of a civil war in 2003 that killed almost 4m people in the world's deadliest conflict since 1945.

The main opposition party, the Union for Democracy and Social Progress (UDPS), accuses the present government of wanting, without a vote, to become rather more permanent than provisional, and says it will keep up the pressure to hold elections. So, unless it soon becomes clear that an election is in the offing, the mood in Congo's crumbling capital, Kinshasa, home to 9m people, may start getting ugly.

Father Apollinaire Malu Malu, the electoral commission's head, says things are on track for all voters to be registered by October. The peace accord allows the government—given Congo's exceptional circumstances—up to two six-month delays if the June 30th deadline is missed.

In its defence the government, brought together from former belligerents, representatives of civil society and elements of the political opposition, rightly says that organising elections in Congo is a logistical nightmare. The country is about the size of western Europe, but with scarcely a decent road outside any of the main towns.

Voter registration started only in late June; by July 10th, over 1m people will have registered. But that leaves another 28m-odd waiting to register, out of a population probably twice that size, most of it in places without the relative efficiency of Kinshasa for running a high-tech electoral system. Despite that, over 9,000 kits—each with a laptop, a digital camera, a fingerprint scanner and a card printer—will be dispatched across the country, reaching their destinations by air, down bumpy bush tracks or on the dugout canoes that ply Congo's rivers. But it is taking time for the first of the 45,000 officials to get to grips with the equipment.

Critics such as the UDPS accuse the government of dragging its feet to hang on to the perks of power. And the government's reaction last week to protests in Kinshasa against the delay was not reassuring. Some 5,000 men from the police and presidential guard beat up demonstrators, while riot police tear-gassed any gathering of people (including this correspondent) almost indiscriminately. The police killed ten people or so and arrested up to 700.

Under the current timetable, Congo should have a referendum on its future constitution in November; a general and presidential election are due by next May. On the eve of the latest protests, President Joseph Kabila promised to speed up preparations for the elections. Doubts about his sincerity may grow.

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South African land

Should reform be faster or steadier?

Jul 7th 2005 | JOHANNESBURG
From The Economist print edition

Frustration is mounting but the arguments are complex

Get article background

AFTER two years of unsuccessful negotiations, the South African authorities are poised to expropriate a white-owned farm in the North West province. But in case this sounds like the start of a horror tale that might replicate events in neighbouring Zimbabwe, rest assured. In this instance the expropriation is definitely legal and the farmer will be fairly compensated. In May, the constitutional court made it clear that land grabs will not be tolerated. And yet, however orderly, there is growing black frustration over the slow pace of land reform. For land is still an emotive and politically explosive issue.

Land reform has been a priority for the ruling African National Congress since it won power in 1994. The 1913 Land Act, which reserved 87% of the country's land for the white minority, was followed by decades of forced removals by successive apartheid governments. So the authorities are buying claimed land and giving it back to its original owners or their descendants, while planning to redistribute 30% of white-owned commercial farmland (22m hectares) to black hands by 2014—on a willing-buyer-willing-seller basis.

A lot has already been done. Out of the 80,000-odd restitution claims, 59,000-plus have been settled, mostly in cities. Rural claims, however, are proving much harder and taking much longer. Siwela Samson, who heads the Tenbosch Land Claim Committee, is seeing some success only after a ten-year struggle. His committee represents about 15,000 people long ago forced off their land in the Mpumalanga province. On June 19th, a ceremony marked the transfer of about 18,000 hectares, under the claim's first phase. Mr Samson admits that, during the decade it took to settle the claim, he at times lost faith in the government's land restitution plan.

Why so slow? Some claims need extensive mapping and a lengthy verification of claimants. Negotiating prices takes time. Redistribution is often tricky. So far the government has had only 3% of land transferred to blacks: the 30% target looks far off. Moreover, South Africa's commercial farming is dominated by large holdings; there is an unresolved debate over whether to encourage small family farms or to create a class of bigger commercial black farmers. Few of the 5% of farms that are sold every year are bought for black farmers. And money has been an issue; less than 1% of the government budget has been allocated to land reform so far.

Some white landowners are accused of being reluctant to sell to black buyers. But a bigger reason for the slow pace of redistribution is that most black farmers can buy only smaller plots, unless they pool their resources. The World Bank's Roger van den Brink points out that South Africa's land-subdivision law and tax system protect large land holdings and make it harder to sell them in smaller units.

In any event, trying to get inexperienced black farmers to become commercially successful is even harder. But creative ideas are being tried. Ian Lourens, whose farm in Mpumalanga is under claim, has agreed with the future owners to form a joint venture. He will provide capital, equipment and training, while the claimants will provide the land. They will share profits until the claimants can manage on their own. The Centre for Development and Enterprise, a think-tank in Johannesburg, says that land reform is not just about land redistribution; the debate should be refocused on urban areas. It argues that most South Africans, 60% of whom live in towns, are keener to have somewhere to live than somewhere to farm: land invasions occur mainly on the edge of cities. It adds that, as farming has become more capital intensive and exposed to international competition, giving farmland to the rural poor will neither help them, nor the country as a whole.

Not so, says the government's Department of Land Affairs: giving opportunities in rural areas, land

redistribution included, is essential, as there are too few jobs in towns to absorb rural migrants.

But all agree that frustration over land reform is dangerous. Exasperation over the government's failure to fulfil its promises on new housing turned into riots in May. Some populist voices are calling for wholesale expropriation, however much costlier and lengthier than the current process. A land summit due at the end of this month may help redirect some of the anger along more practical lines.

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Iraq

A voice for the insurgents

Jul 7th 2005 | BAGHDAD
From The Economist print edition

The Iraqi government and its American allies are trying to split the insurgency

A VIDEO of masked gunmen released to al-Jazeera, the region's most influential satellite television channel; a bootleg DVD featuring burnt-out humvees set to religious chanting; a claim of responsibility for an attack posted on one of the internet's ever-migrating Islamist websites. These are all the outside world sees of most of Iraq's myriad insurgent groups. So it is hard to work out what connection, for example, the Islamic Jihad Brigades of Muhammad's Army has to the Armed Vanguards of Muhammad's Second Army, or whether a particular movement has a nationwide network with thousands of disciplined members or three self-promoting cousins with a video camera.

To some extent this very amorphousness helps the rebels, for it enhances their mystique as an omnipresent force of shadowy avengers. But what if Iraq's government wanted to seek out people to negotiate with?

It has issued a tentative welcome to the news that two of the better-known insurgent groups have jointly named an official spokesman. The announcement, on the internet, said that the Islamic Army of Iraq and the Army of the Mujahideen, two groups thought to be linked to Saddam Hussein's Baath party and which have issued joint communiqués in the past, had named Ibrahim Youssef al-Shammari as their official spokesman. He said he would “silence those who would speak in the holy warriors' name”—presumably a rude reference to Ayham al-Samarrai, a Sunni politician who recently presented his own front organisation to voice rebel demands. However, the bona fides of the previously unheard-of Mr Shammari are equally hard to evaluate; so far he has limited his public-relations outreach to telephone conversations with al-Jazeera. But, in the absence of any vigorous counter-claims, he is probably a genuine spokesman.

Does his apparent nomination as the political voice of an insurgent group suggest that at least some fighting groups want to open negotiations? Perhaps. But the barriers are high. Much has been made of a recent off-hand remark by Donald Rumsfeld, the American defence secretary, which seemed to indicate extensive contacts between American officers and Iraqi rebels. But other American officials say that, while often approached by people claiming to have been sent by the insurgents, they pass them on to the new Iraqi government. If the Americans started to cut private deals with the insurgents, this would undermine the Iraqi government and infuriate the main Shia parties in government, among whom a twitchy fringe has always suspected the Americans of being secretly in league with the Sunni Baathists all along. Some Iraqis in government suspect that the Americans have already opened a back-channel, and they are not happy about it.

Mr Shammari, for his part, has denied that the Americans are indeed quietly talking behind the scenes to his lot of insurgents, who, he says, would nonetheless welcome a public initiative from the American Congress—thereby implying that the current Iraqi government cannot be taken seriously as a negotiating partner. Meanwhile, though the previous interim prime minister, Iyad Allawi, himself a former Baathist, tried to reach out to some of the insurgents, the present Shia-dominated government led by Ibrahim al-Jaafari says it is only in the initial stages of making contact. One problem, it seems, is that they still do not know who's who in the Sunni areas.

And what might those of the insurgents who seem interested in talks like to discuss? Among their prime demands are the recreation of the old Iraqi army, the payment of pensions to former officers and the reversal of “de-Baathification”. They also usually preface those demands with calls for a timetable for foreign forces to withdraw: a non-starter as far as the Americans and the Iraqi government are concerned. Moreover, Dr Jaafari's representatives say he will cut deals only with rebel groups who have never attacked Iraqis and who stopped attacking Americans after the general election on January 30th. This rules out most of them as interlocutors, though one government spokesman said that groups

interested in parleying should not be examined under a “microscope”.

The government's big hope is for the Jordanian Islamist, Abu Musab al-Zarqawi, to be knocked out of the equation. His network is thought responsible for most of the suicide volunteers whose attacks so poison the atmosphere; his group's apparent strategy—unconditional *jihad* against both American occupiers and Shia “heretics”—leaves no room for compromise. Hoping that the rebels with more worldly goals are tiring of their partnership with Mr Zarqawi, the Americans are encouraged by reports of clashes between foreign Islamists and more tribally-based Iraqis near the northern town of al-Qaim. But until now, however diverse in ideology, the assorted groups have refused to betray each other. If that process were to start, the Iraqi government would have a much better chance of imposing its authority.

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The Philippines

Under fire

Jul 7th 2005 | MANILA
From The Economist print edition

AFP

There is no good alternative to President Gloria Macapagal Arroyo, despite what look like serious errors

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JUDGING by past precedent, Gloria Macapagal Arroyo's days as president of the Philippines should be numbered. By her own admission, she telephoned an election official amid the counting of votes in last year's presidential election, in what could be construed as an attempt to rig the vote. In 1987, similar suspicions of ballot tampering led to the demonstrations that brought down Ferdinand Marcos, the Philippines' strongman of 20 years. Meanwhile, Mrs Arroyo's husband, son and brother-in-law have been accused of pocketing bribes from illegal gambling syndicates—exactly the charge that prompted the Philippines' second “people power” revolution, against Joseph Estrada, in 2001. Despite this record, however, most Filipinos seem disinclined to oust their president this time round.

The claims of election fraud stem largely from a long series of recordings of a man, allegedly election commissioner Virgilio Garcillano, speaking by mobile phone to various people about the progress of the vote count. In one tape, a woman, said to be Mrs Arroyo, asks about provinces where her henchmen were accused of subtracting from the opposition's votes while padding her own tally. In response, the man says, “What they did to raise yours—it was done well.” Mrs Arroyo's spokesman at first claimed the tape was doctored, and that no such conversation had taken place. But Mrs Arroyo herself subsequently admitted telephoning an unnamed election official, without confirming or denying the authenticity of the tapes. She says she spoke to him not to rig the vote, but rather to guard against any such attempt.

According to a recent poll, 59% of Manila residents believe that the president was trying to fiddle the ballot, while only 29% accept the claim that she was trying to protect her votes. But only 18% of those polled want her to resign (earlier polls, it is true, had a higher figure). Less than 1% want another “people power” revolution. A far higher proportion—20%—want the country to put the episode behind it.

The president's detractors have not managed to turn out more than 10,000 demonstrators so far, compared with the hundreds of thousands who rallied against Presidents Marcos and Estrada. The opposition lacks leaders with the appeal of Corazon Aquino, who took over from Mr Marcos, or of Mrs

Arroyo herself, who was vice-president and succeeded Mr Estrada.

Mrs Arroyo's main rival in the suspect election, Fernando Poe junior, died last year. Mr Estrada, who never accepted his own removal, is still popular with poorer Filipinos, but is under house arrest while standing trial for corruption. He has endorsed Susan Roces, Mr Poe's widow, as a potential figurehead for the opposition. But she has no political experience and no obvious following. Neither the Catholic church nor the army, which were both instrumental in the past two “people power” uprisings, has turned against Mrs Arroyo. A few Catholic bishops have called on her to step down, but the leading Catholic prelate in the country, Archbishop Gaudencio Rosales of Manila, has advised his flock to respect the constitution.

The constitution does provide for a president's removal from office for misconduct. The House of Representatives must first pass a motion of impeachment, whereupon the Senate would sit as a glorified jury in a trial presided over by the chief justice. The House is due to take up such a motion when it returns from recess on July 25th. Mrs Arroyo has said she would welcome impeachment as an opportunity to clear her name. But that is disingenuous: her allies dominate both houses. Moreover, no one seems to think very highly of the vice-president, Noli de Castro, a former news anchorman who is first in the line of succession. So far, only one congressman has deserted the president's camp.

Mrs Arroyo said on July 7th that she herself would not step down but that she had asked her entire cabinet to do so. This followed some other dramatic announcements apparently designed to improve her standing. Last week, she revealed that her husband would be leaving the country indefinitely, to preclude any further talk of influence peddling. Her son, a congressman, is taking a leave of absence and going with him. The agriculture secretary, Arthur Yap, has stepped down to face charges of tax evasion.

The departure of the cabinet is designed to let Mrs Arroyo pursue some big legislative plans. She hopes to amend the constitution, to transform the Philippines from a unitary state with a presidential system into a federation with a parliamentary one. She wants to balance the budget by the end of her term in 2010. Last week, the Supreme Court unintentionally highlighted the importance of the president's fiscal rectitude by suspending a new law empowering her to raise the rate of value-added tax (VAT). The stockmarket plunged by almost 5% in a day.

That hints at Mrs Arroyo's greatest strength amid all the current scandals. During the ructions that unseated Presidents Marcos and Estrada, many protesters were motivated not so much by outrage at suspected vote-rigging or corruption, which are unfortunate facts of life in the Philippines, but by a broader concern that their leaders were driving the country into the ground. Mrs Arroyo, on the other hand, although by no means a model president, has taken sensible steps to improve the country's finances, reform the bureaucracy and—ironically—overhaul the electoral system. Whatever turns out to be the truth of the allegations dogging her, for now she looks like a bulwark against chaos, not an agent of it.

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Malaysia

A storm in a teapot

Jul 7th 2005 | KAMPUNG BATU 13
From The Economist print edition

The government gets tough on apostasy

AYAH PIN, the leader of an inter-faith cult in the Malaysian state of Terengganu, makes no bones about his divinity. He owns everything on the planet, he patiently explains to visitors, as the earthly incarnation of what he calls the Sky Kingdom. To back up his claims, he has built a giant teapot and an even bigger yellow umbrella, in accordance with blueprints from on high. His followers currently number a few thousand, he says, but the rest of humanity will eventually come round.

The government of Terengganu, however, remains sceptical. During the 1990s, it locked up four of his Muslim followers (there are also Christians, Buddhists and Hindus) for attempting to renounce Islam—a crime in most Malaysian states. It has repeatedly ordered the demolition of the teapot and umbrella, for violations of the building code. In 2001, an Islamic court jailed Ayah Pin himself for 11 months, for deviancy. On July 3rd, police raided his compound and arrested 21 of his followers. Ayah Pin, whose real name is Ariffin Mohammad, escaped, doubtless thanks to a heavenly tip-off.

The national government of Malaysia, headed by the United Malays National Organisation (UMNO), says that it believes in persuasion rather than coercion in matters of religion. But it refuses to endorse the idea that Muslims should interpret and observe their faith as they see fit. It is tracking 22 sects it deems deviant, with some 22,800 members between them. When some of Ayah Pin's Muslim followers appealed last year to the Federal Court, Malaysia's highest, to recognise their right to profess the religion of their choice, the judges ducked the issue. Meanwhile, in states like Terengganu, also run by UMNO, repressive laws against heresy and apostasy remain on the books, and officious local functionaries occasionally enforce them.

Nik Aziz Nik Mat, the leader of the Islamic Party of Malaysia, the country's main opposition, is not satisfied with this muddle. He says the biggest heretics are the leaders of UMNO, who pay lip service to Islam, without following through consistently. Ayah Pin, however, is more open-minded. His followers are free to worship as they please, since the Sky Kingdom is above petty matters of doctrine and ritual. No wonder the authorities think he is mad.

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China

Uncooking the books

Jul 7th 2005 | BEIJING
From The Economist print edition

A spirit of openness in official China

Get article background

CHINA'S Communist government is skilled at manufacturing heroes. Among its recent creations is "Iron-faced Li", a man who has dared to violate a deeply ingrained tradition of bureaucratic secrecy by publicly naming and shaming powerful ministries for mis-spending funds. He is China's auditor-general, Li Jinhua, who last December helped fuel the media cult surrounding him by shedding televised tears after being named China's top economic personality of the year.

Mr Li's fans were not disappointed last week by his annual report to China's legislature on the scrutiny conducted by his National Audit Office (NAO) of the central budget and other government finances. The report gave details of $1.1 billion in funds mis-spent by central departments, and $8.6 billion misused by the debt-clearing agencies at the forefront of China's banking reforms. China's leaders have good reason to burnish the image of the 62-year-old son of a pastry chef. His reports fit the style of a new leadership under President Hu Jintao that began taking over in 2002. Mr Hu has been trying to gain public support by showing resolve to curb corruption and displaying sympathy with the marginalised. There has been speculation that Mr Hu also sees the audit reports as a useful way of targeting opponents, although evidence for this is thin. Mr Li took up his post in 1999 but only began giving his reports real bite as Mr Hu consolidated his power (they have been published in full since 2003).

Another good reason for officially lionising Mr Li is simply that China's finances are an opaque mess. The legislature, or National People's Congress, rubber-stamps a budget in March that delegates have had a chance to review for only a few days beforehand. The budget gives vague descriptions of how money will be spent and, oddly, covers a financial year that begins three months before the document is unveiled. Ministries do not publish details of their budgets. Policymakers lack reliable data on an array of liabilities, such as bad loans and local government debts, that could threaten financial stability.

The Ministry of Finance, which is responsible for managing the central budget, was itself a conspicuous subject of this year's report. Among its errors was a lack of control over the budgets of the People's Bank of China (the country's central bank) and the main state-owned television and radio services. It was also criticised for failing to make budgets detailed enough. Some 13% of funds audited in the four asset-management companies set up by the ministry to handle the state-owned banks' non-performing assets were found to involve irregularities. One of the companies was accused of having made up 3,983 fictional employees, for which it obtained nearly $24m from the ministry to cover salaries and other benefits. A few years ago, this sort of public criticism would have been simply unthinkable.

Yet there are limits to Mr Li's *glasnost*. The Communist Party itself has yet to be mentioned in his broadsides, though it, too, is supposed to be subject to the NAO's scrutiny. There has been no mention of the police, either. (The armed forces have a separate, more secretive, auditing system.) Mr Li did acknowledge that 760 people had been disciplined within the party or subjected to criminal proceedings for wrongdoings raised in his report last year. But he did not mention any names, state how many had actually been jailed, or give any other details of punishments. In 2000, the newly appointed Mr Li said it would take his auditors about three years to put a stop to major malpractices in central departments. The iron-faced hero, it seems, was a little over-confident.

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Japan

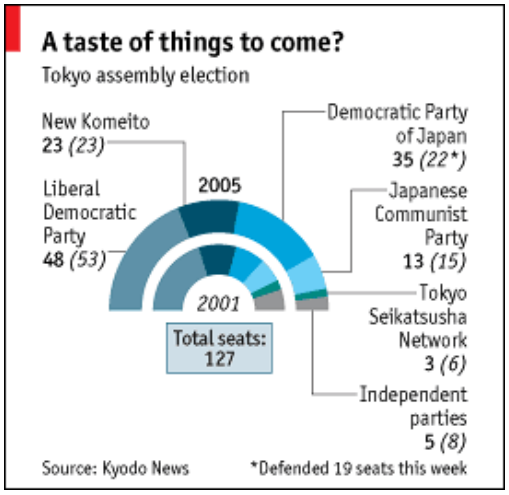
A power shift?

Jul 7th 2005 | TOKYO
From The Economist print edition

Between Tokyo's elections and postal reform, the opposition had a great week

Get article background

HIS future had looked grim, but Katsuya Okada, Japan's opposition leader, scored two big wins this week—one without even trying. First, his Democratic Party of Japan (DPJ) stunned everyone on July 3rd, making huge gains in an election for Tokyo's local assembly. The DPJ sharply increased its representation, from 19 to 35 seats. Two days later, Mr Okada and the DPJ were able to gloat while the Liberal Democrats (LDP) split into warring camps over bills to privatise Japan's post office and related bank and insurance arms. Junichiro Koizumi has staked his career on this reform, but much of the prime minister's party defied him, and the bills squeaked through the lower house by only five votes. Mr Koizumi is braced for an upper-house battle; Mr Okada has fresh clout.



The Tokyo contest was the last big battle between the DPJ and the LDP before the next national election, due by 2007. And although the DPJ did not win a majority (see chart), it impressed Japan's media and gained momentum. “The DPJ leaps ahead,” gushed the *Tokyo Shimbun*, a daily newspaper, on its front page. Japanese politicians take their cues from the media, says Kunji Okue, a political analyst at Dresdner Kleinwort Wasserstein, an investment bank, and “if all the newspapers say it's a win, it's a win.” The question now is whether the DPJ can convert this head of steam into an actual win in the next general elections instead of settling for the media kind yet again.

Mr Okada says that the DPJ is at last ready for this next step: “We have a common goal now,” he claims. “It is to take power, to become [Japan's] ruling party.” Because the LDP has ruled Japan almost continuously since 1955, such a change of power could liven up Japanese democracy and spur many reforms. A closer look at the Tokyo elections, however, suggests that the DPJ still has further to go.

To beat the LDP, the DPJ must not only do better in rural areas, which are over-represented in parliament and where the LDP is strongest, but will also need to crush it in the cities, which means finding an answer to New Komeito, the LDP's coalition partner. New Komeito, backed by a committed block of urbanite Buddhist voters, not only does well in the districts it contests—it won 23 seats in Tokyo this time, as it had in 2001—but also backs LDP candidates for other seats, which eats further into the DPJ's urban strength. This week the LDP won only five fewer seats than in 2001, even though Mr

Koizumi had 80% popularity ratings back then.

Moreover, this week's good showing will probably help Mr Okada hang on to his job as party leader, which paradoxically could hold the DPJ back. Many younger MPs do not think he is the man to unite the party and choose clear themes. And even among DPJ voters, he is less popular—by 19% to 24%—than Shinzo Abe, the front-runner to succeed Mr Koizumi as LDP leader in September 2006.

Unless Mr Okada can raise his game, therefore, the DPJ may still need lots of outside help to win power. Short of another economic recession, that means some sort of collapse of the ruling coalition. New Komeito could probably swing the next election to the DPJ, if it wanted to. But its members say they will stick with the LDP for now. Or the LDP itself could disintegrate, perhaps during a leadership contest in 2006, or much sooner if Mr Koizumi loses the post office vote in the upper house this summer.

Most political watchers, however, still reckon that the coalition's upper-house members—despite holding a narrower majority than in the lower house—will find enough party discipline to pass the postal privatisation bills in August. Mr Koizumi has threatened to dissolve parliament if they do not, and the party does not want to face an election in disarray, especially against a reinvigorated DPJ. Another paradox, therefore, for Mr Okada: his victory in Tokyo may be just enough to focus the LDP's attention, and deliver Mr Koizumi his coveted postal reform.

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The Shanghai Co-operation Organisation

Suppression, China, Oil

Jul 7th 2005
From The Economist print edition

What the SCO really stands for

TWO days before the summit, on July 5th, of the Shanghai Co-operation Organisation (SCO) in Astana, Kazakhstan's capital, a communiqué issued by China and Russia hailed the regional alliance for its role "in establishing a just and rational new international political and economic order". Judging from the activities of the member states (China, Russia, Kazakhstan, Kirgizstan, Tajikistan and Uzbekistan), three principles define that new order: slaking China's thirst for energy, protecting member states as they tyrannise dissidents and curbing America's influence in the region.

Driven by Chinese demand, energy business in the SCO, often nicknamed the "Shanghai Six", is booming. On his trip to Kazakhstan, China's president, Hu Jintao, opened negotiations on analysing the possibility of a gas pipeline connecting China and Kazakhstan; a similar oil pipeline is due to be completed by December. The SCO invited Iran, India and Pakistan to attend as observers; China hopes to share in the benefits of a proposed pipeline that will bring gas from Iran to India, via Pakistan. At the Astana summit, SCO leaders reaffirmed their interest in strengthening such links.

These ties help explain why the SCO has provided staunch support to Islam Karimov. The Uzbek dictator massacred hundreds of his own citizens in Andijan in May; he also, however, signed a $600m joint energy exploration deal with the Chinese shortly afterwards. But more than the desire to protect investments lies behind the SCO's support of Mr Karimov. Member states are concerned about their own dissidents. Russia applauds Andijan as part of a war against terror because it has long represented its conduct in Chechnya in the same light. China, for its part, has secured much-needed Uzbek and Kazakh co-operation in dealing with its restive Uighurs in Xinjiang province.

On the eve of the summit, therefore, the SCO's secretary-general, Zhang Deguang, defended the massacre as a blow against terrorism and called for enhanced regional security co-operation. "We have not come across a situation," he said, implicitly responding to western calls for an international investigation, "where we could not tell who was the terrorist and who was the freedom fighter." The SCO called for "non-interference in the internal affairs of sovereign states". That non-interference is used to justify a new extradition agreement, whereby Kirgizstan will return Uzbek refugees wanted by the government in Tashkent. All this sends a clear message: members of the SCO will brutally oppress their citizens, if they feel the need, and the outside world has no right to interfere.

Telling outsiders—meaning, mainly, Americans—not to interfere, however, is only part of it. The SCO wants to rid the region of the American military presence altogether. This week it called for a deadline by which the America-led coalition in Afghanistan should remove its airforce bases in Kirgizstan and Uzbekistan. Ostensibly, the SCO made the call because Afghanistan is becoming more stable. But Russia and China would be keen to fill the vacuum. Chinese researchers have arrived in Uzbekistan to build an "anti-terrorism centre" there, and Russian troops will train with the Uzbek army later this summer. More will probably follow. In time, the SCO's effectiveness may well be harmed by Central Asian resentment at being treated, once more, as the rope in a tug-of-war between Russia and China. But a struggle for the mastery of Central Asia is again unfolding.

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Afghanistan

Zabul's no Kabul

Jul 7th 2005 | QALAT
From The Economist print edition

In Afghanistan's badlands, things are getting worse, not better

THE 19th-century British fort that dominates the skyline above Qalat offers an easy reference point for low-flying Apache helicopters heading for the America base near the town, the capital of Afghanistan's southern province of Zabul. Yet despite being backed by impressive foreign muscle, the government's control in Qalat barely reaches the city limits. On the Pakistani border, deep in the conservative Pushtun belt from which Mullah Omar's movement first emerged to gain control of Afghanistan, Zabul remains Taliban country. Security has deteriorated so badly on the Kabul to Kandahar highway that 17 new emplacements were built along a 60-kilometre (40-mile) stretch north of Qalat in June. The road is beginning to look like the Maginot line.

Since March, the level of violence in south-eastern Afghanistan has reached and then surpassed the levels of the same time last year. The shooting down of a Chinook helicopter carrying 16 American personnel in Kunar province on June 28th was the biggest single success the Taliban and their al-Qaeda allies have enjoyed against American forces since the war of 2001. After the optimism that followed the low levels of violence during last year's presidential elections, is the tide turning? As the pockmarked walls of the British fort attest, America wouldn't be the first foreign power to lose its way in Afghanistan.

Despite claims that support for the Taliban is weak or extracted under duress, support in rural Zabul, at least, remains high. “In the rural areas the people are uneducated and they follow what the mullahs tell them,” says Mohib, an English teacher in Qalat. “The rural people are conservative and they don't like foreigners.” Locals say Zabul has only one functioning high school for boys: a campaign of arson and intimidation has closed all but five of 170 schools in the province.

Violence is also expected against workers and candidates in September's parliamentary elections. Ragabea Ranjba, a female candidate, accepts she will have little opportunity to present her manifesto. “We can't campaign because there is no stability here,” she says.

But despite the siege mentality evident in Qalat, the American and Afghan government forces claim to have fought and won several large battles in the south recently. These have been engagements on a scale rarely seen since 2002. Some 600 people are said to have died since March, three quarters of them alleged insurgents. The Taliban have repeatedly concentrated their forces, bringing together as many as 200-300 fighters and aiming to seize and hold entire districts for short periods. It is a bold tactic, which has been repeatedly punished with airpower. In late June, the Taliban held Mian Nishin

district, north-west of Qalat, for two days, losing 178 fighters according to the government.

The causes of these large-scale engagements appear to be twofold. The latest rotation of American forces in the south has brought in the tough 173rd Airborne Brigade. Their ongoing Operation Determined Resolve has been an attempt to put the insurgents on the back foot ahead of the elections, by pushing into areas of the south hitherto regarded as Taliban safe havens. Yet it is also clear that the Taliban promise of a “spring offensive” was no bluff. Since March, they have showed themselves to be a still functional and well-equipped movement without any apparent shortage of manpower. A recent line proffered to the press that this is the last gasp of the Taliban rings hollow. Taliban fighters are clearly crossing and re-crossing from Pakistani border areas in large numbers. In the police chief's office in Qalat, General Abdul Sabur Al-Allahya casually lists five locations he claims are Taliban training camps on the Pakistan side of the border. Afghan officials accuse parts of the Pakistani administration and intelligence services of sympathy, even collusion, in training, logistics and intelligence support.

Other parties with a more clearly vested interest in instability are not hard to find in southern Afghanistan. From the vast opium business through to local warlords and tribal bodies opposed to disarmament and the imposition of strong central government, many would like to maintain the status quo. To this must be added a growing frustration amongst ordinary Afghans with the pace of reconstruction and the corruption that is taking hold in the organs of government. The blood-letting seems unlikely to abate ahead of September's elections, or indeed for a long time after that.

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Mobile phones and development

Calling an end to poverty

Jul 7th 2005
From The Economist print edition

Still Pictures

Mobile-phone firms have found a profitable way to help the poor help themselves

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ALL eyes are on what governments can do to end poverty, with aid, debt relief and trade top of the agenda at this week's G8 summit. But what about the role that business can play—and, in particular, technology firms? It is increasingly clear that, when it comes to bridging the "digital divide" between rich and poor, the mobile phone, not the personal computer, has the most potential. "Emerging markets will be wireless-centric, not PC-centric," says C. K. Prahalad, a management scholar and author of "The Fortune at the Bottom of the Pyramid", a book that highlights the collective purchasing power of the world's 4 billion poorest people and urges firms to try to profit from it.

Mobile phones have become indispensable in the rich world. But they are even more useful in the developing world, where the availability of other forms of communication—roads, postal systems or fixed-line phones—is often limited. Phones let fishermen and farmers check prices in different markets before selling produce, make it easier for people to find work, allow quick and easy transfers of funds and boost entrepreneurship. Phones can be shared by a village. Pre-paid calling plans reduce the need for a bank account or credit check. A recent study by London Business School found that, in a typical developing country, a rise of ten mobile phones per 100 people boosts GDP growth by 0.6 percentage points. Mobile phones are, in short, a classic example of technology that helps people help themselves.

But despite rapid subscriber growth in much of the developing world, only a small proportion of people—around 5% in both India and sub-Saharan Africa—have their own mobile phones. Why? The price of handsets is the "biggest obstacle" to broader adoption, says Alan Knott-Craig, boss of Vodacom, which runs networks in five African countries. Azmi Mikati of Investcom, which runs networks in Africa and the Middle East, estimates that the number of users would double in those markets if the cheapest handset cost $30 instead of $60.

Ringing the changes

Handset-makers earn most of their profits from fancy phones sold to consumers in rich countries, where on average a handset costs around $200 (before operator subsidies). But as markets have become

saturated in the rich world, manufacturers have started to realise that their future growth depends on catering to the needs of developing nations. As a result, they have been working with operators to develop new extremely cheap handsets and to boost adoption in the poor world.

Several operators from developing countries teamed up earlier this year under the auspices of the GSM Association, which promotes the use of GSM, the world's dominant mobile-phone standard. They invited the handset-makers to bid for a contract to supply up to 6m handsets for less than $40 each. The contract was won by Motorola. Delivery of handsets began in April. The low cost is not due to cross-subsidy from high-margin handsets or “corporate social responsibility” funding, insists David Taylor of Motorola. “We do make a margin—a much smaller margin, but it is still a margin,” he says.

This week the procurement process began for more handsets, to be delivered from next January. As well as letting smaller operators pool their bargaining power, this scheme aims to draw manufacturers' attention to the needs of developing countries. “This was the first time that emerging-market operators had come together,” says Ben Soppitt of the GSMA. Each operator is small, but together they represent a big market. “We believe we can increase the market by 100m-150m customers a year for five to ten years if we can get the affordability right,” he predicts. That means encouraging handset-makers to design new extremely cheap phones on which they can still turn a small profit.

Such a phone cannot simply be a cut-down version of an existing handset. It must be very reliable and have lots of battery capacity, as it will be used by people who do not have reliable access to electricity, says Mr Taylor. Motorola's low-cost handset has a standby time of two weeks. And the handset must conform to local languages and customs: Motorola's handset, for example, includes a football game in Africa, but a cricket game in India.

Nor can the makers skimp on design. Kai Oistamo of Nokia, the world's largest handset-maker, notes that people in poor countries have to spend a far larger proportion of their income than those in the rich world to buy even the cheapest handset. “So looks and brand are highly important—it is much more of a status symbol in those societies,” he says. And it is wrong, points out Mr Prahalad, to assume that consumers in poor countries will not be interested in fancy features such as music-playback. Since they cannot afford multiple devices—an iPod, a PC, a PlayStation—they may want more from their mobiles.

As handset-makers respond to this new market, prices will continue to fall. “We will give you the volumes so that you can continue to drive down prices,” promised Sunil Mittal, boss of Bharti, a big Indian operator, at a recent industry conference. On June 29th Philips, a Dutch electronics firm, announced a new range of chips designed to take handset costs below $20.

Lower prices will make a second barrier ever more apparent: high taxes and duties imposed by many governments on handsets and services, often just as growth in the sector starts to take off. “It does seem strange for countries to say that telephone access is a public-policy goal, and then put special or punitive taxes on telecoms operators and users,” says Charles Kenny, an economist at the World Bank. “It's a case of sin taxes on a blessed product.”

In Turkey, new subscribers must pay a special tax of 20 new liras ($15) for a connection. A sales tax of 18%, plus a special communications tax of 25%, is added to all mobile bills. Uganda has just imposed a 10% tax on mobile phones. In Afghanistan, telecoms taxes account for 14% of government revenue, says Mr Kenny. In Bangladesh, the government has just imposed a tax of 900 taka ($14) on all new connections, in addition to an import duty of 300 taka levied on all imported handsets.

In big markets, such as Brazil, handset-makers have set up local factories to avoid import duties. That will not pay in smaller, poorer places. To avoid taxes and duties, many mobile operators in sub-Saharan Africa do not supply handsets, but rely on customers to get them on the black market, says Mark Burk of Informa, a research firm.

Yet there is anecdotal evidence that reducing taxes on handsets can boost government revenues. People would rather pay a small tax on a legal handset than no tax on a smuggled one that cannot be returned if it goes wrong. There are some hopeful signs: India cut its import duty on handsets to 5% last year and plans to scrap it altogether. Mauritius recently cut its taxes on handsets to boost adoption.

The GSMA is now making a 50-country study that will, it hopes, provide conclusive proof of the benefits of cutting taxes on mobile phones. The aim, says Mr Soppitt, is to show that a “win-win-win” scenario is possible, in which customers get cheaper access, manufacturers and operators sell more handsets and airtime and governments raise their tax revenues. (Oh, and the “digital divide” vanishes, too.) With its new focus on low-cost handsets, the industry is doing its part to extend access to communications technology. Now governments must do their part, too.

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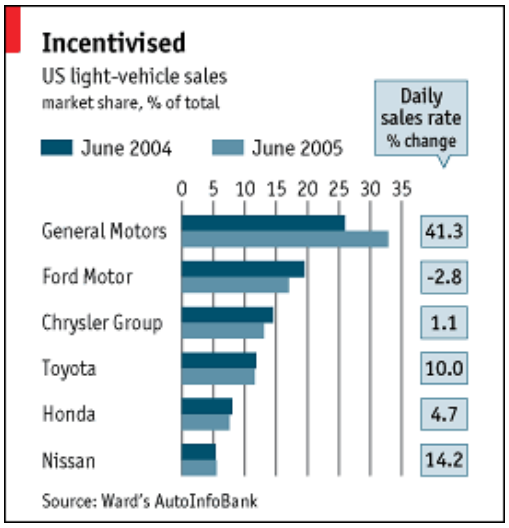
American carmakers

Hooked on discounts

Jul 7th 2005 | DETROIT
From The Economist print edition

The price war in Detroit has hotted up, with a new wave of sales incentives



IT HAS been 30 years since a desperate, fast-sinking Chrysler turned traditional vehicle marketing upside-down. In a brash ad campaign, a former sportscaster, Joe Garagiola, blared out, “Buy a car, get a cheque.” Those $50-500 discounts kept Chrysler alive until a federal bailout came along. Now Chrysler plans to go one better. In the coming weeks, it will be giving customers cash, while also letting them buy their vehicles for the same price as company employees.

Bloated by an estimated 15-20% excess capacity, America's car market is more competitive than ever, and foreign brands have seemed to be gaining the upper hand. Last month, General Motors (GM) tried to change this with its “Employee Discounts for Everyone” offer. This ladled an extra $450 on average on to GM's typical incentive package. That represents a lot of lost money for a business that lost $1.1 billion in the first quarter of this year. As a result, a buyer in the mid-west might buy GM's Chevrolet Silverado 1500 full-size pickup truck for more than one-third off the retail price. No wonder GM's sales soared by 41% in June, lifting its market share to 33%—its highest since 1994.

When GM decided to continue the offer, the American Chrysler arm of DaimlerChrysler had no choice but to respond with a deal of its own, “Employee Pricing Plus.” (Even before this new offer, a typical Chrysler customer drove off with $3,975 in give-backs last month.) So, too, Ford, with its “Family Plan.” Like GM, the two carmakers will exclude only a few of their best-selling vehicles from the new offers.

Next month's sales should be strong for all three. But what about the rest of the year? “Payback” is a word now heard often in automotive circles, as motorists pull forward planned purchases to exploit the latest round of incentives. But when the discount campaigns end, some fear, sales could collapse.

Still, GM reckons its offer has lured in about 150,000 customers who did not previously own or want to trade in a GM vehicle. That is something it could not accomplish with its recent wave of new products, such as the Pontiac G6 sedan.

The big long-term challenge, says Joe Phillippi, of AutoTrends, a consultancy, is to get back to “rational pricing”—ie, covering total costs, not just marginal ones. Because of all the give-backs, the price paid for

a Detroit model has barely risen since the late 1990s. Ultra-reliable Japanese vehicles, on the other hand, have commanded steadily higher prices in America, even after the bigger, but still modest, incentives that the Japanese carmakers have felt obliged to offer.

Chrysler's famed ex-boss, Lee Iacocca, once likened rebates to narcotics. Recent trends suggest he was right. Even Mr Iacocca seems addicted: he is to star in new ads touting Chrysler's latest offer.

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Volkswagen

An icon under fire

Jul 7th 2005 | BERLIN
From The Economist print edition

A corruption scandal calls into question the German business model

EPA

Losing its shine

AS A symbol of Germany's traditional consensual model of business, there is none better than Volkswagen (VW). Europe's biggest carmaker is a famed practitioner of the *Mitbestimmung* system of co-operation between managers and workers. A high percentage of its workers are unionised. Gerhard Schröder, Germany's chancellor, is a former member of its supervisory board and the government of the state of Lower Saxony is its biggest shareholder, making it the most politically sensitive of the country's corporations.

Hence the excitement now gripping Germany over an unfolding bribery scandal at VW. Many of the details are still uncertain, but the allegations of fraud and improper deals between representatives of management and workers to secure union support for cost-cutting and other unpopular measures seem grave enough for many Germans to lose any remaining faith in co-determination—already badly shaken by the country's economic woes.

Last week, the Brunswick state prosecutor announced an investigation into whether Helmuth Schuster, an ex-head of personnel at VW's Skoda unit who unexpectedly quit last month, and another unnamed employee, were involved in fraud. Mr Schuster was an adviser to Peter Hartz, VW's personnel chief, and a business partner of Klaus Volkert, VW's powerful works council chief. Late last week Mr Volkert quit amid allegations of wrongdoing connected to Mr Schuster. VW called in KPMG to look afresh at its books.

The story then took a political turn. On July 5th, Mr Schröder defended Mr Hartz by praising the reform of Germany's labour-market laws that bears his name. On the same day, Mr Hartz and VW's works council denied newspaper reports that VW managers had bought off senior union leaders, for instance with trips to Brazil.

Under German law, workers can form a works council that has a role in management decision-making. Worker and union representatives are entitled to half of the seats on the supervisory board—which oversees the management board—in corporations with over 2,000 employees and to one-third of supervisory board seats in firms with 500-2,000 workers.

Critics argue that this co-determination discourages bosses from taking tough measures that might annoy the board's labour representatives. It slows decision-making. It tends to deter foreign investors. And it may tempt managers to buy labour's support. “The more influential the works council, the stronger the temptation to make some arrangement with labour,” says Peter von Blomberg of Transparency International, an anti-corruption group.

But some executives, including Jürgen Schrempp, boss of DaimlerChrysler, another carmaker, like the system. Workers accept tough measures more readily if they are part of the decision-making, they say.

The German government is now forming a committee to examine reform of co-determination. Last year the Confederation of German Employers demanded change. Yet, although it was expected to call for the end of co-determination, says Martin Höpner, at the Max Planck Institute for the Study of Societies in Cologne, in the end its main demands were for smaller supervisory boards and for firms of all sizes to be able to decide on the number of their board seats allocated to unions.

The scandal may have a silver lining for VW. Bernd Pischetsrieder, the chief executive, and his ally,

Wolfgang Bernhard, are trying to make the firm more “Anglo-Saxon”, with more focus on performance. Thanks to labour's power within the firm, VW workers earn about 20% more than the average salary of workers in German car firms. Mr Bernhard, who recently joined VW from DaimlerChrysler, is putting the finishing touches on another round of cost-cutting. Adam Jonas, an analyst at Morgan Stanley, says the alleged scandal may be just what the management needs to be able to push through the changes it wants. How convenient.

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Bankruptcy

Round and round

Jul 7th 2005 | MEXICO CITY
From The Economist print edition

A cross-border battle over a bankrupt Mexican satellite provider

YOU know you are in bad shape when the question is not whether to file for bankruptcy, but where. Satmex—as its name suggests, a Mexican satellite communications firm—faces just such a dilemma. At the end of May, a group of bondholders, who together hold some $500m of the firm's debt that came due last year but was not repaid, filed a petition in a federal court in New York to force Satmex into involuntary bankruptcy. They did this despite a plan to lend the company more money so that it can launch a new satellite, which the investors believe will make the firm profitable again. Their motivation was to stop a bankruptcy filing in Mexico, known as a *concurso*. A few weeks later, Satmex filed there nonetheless.

The creditors are battling against Mexico's government, which owns about a quarter of Satmex and regulates the satellite industry, and is also a creditor of a holding company that owns Satmex. When the firm was privatised in 1997, the government let the purchasers, Loral Space & Communications, an American satellite firm based in New York and incorporated in Bermuda, borrow about $200m to help pay the $800m price. This debt was put at the level of the holding company, because, claims one of Satmex's creditors, the sale was made at above the market price.

Under American law, the bondholders' debt gets priority. Under Mexican law, it is not clear what will happen. Due to controversy over the privatisation of Mexico's banking system in the 1990s, there is intense pressure to ensure that the government's debt gets priority. But some American investors—including hedge funds—say that the firm's decision, in late June, to file for *concurso* in Mexico will negatively impact investor confidence in the country. Moreover, the creditors say that the Mexican government is largely responsible for Satmex's current straits. Shortly after privatising Satmex, the government liberalised the process for awarding satellite licences, ending Satmex's effective monopoly on providing satellite services to Mexico.

As *The Economist* went to press, Satmex faced a July 7th deadline to respond to the involuntary bankruptcy petition in America. Unless the American court is persuaded to cede jurisdiction to Mexico, the legal battle will drag on simultaneously in both countries.

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Podcasting

Fiddly no longer

Jul 7th 2005 | SAN FRANCISCO
From The Economist print edition

Apple introduces yet another new medium to the mainstream

Get article background

"PODCASTING" is a potentially misleading term. It originally had nothing intrinsically to do with Apple's iPod music-player—and it is nothing like traditional broadcasting. Instead podcasts, which first appeared last year, are audio files that professionals and amateurs alike create and publish on a website, for downloading by anyone who wants to listen. So far, any confusion about the term or the process has not mattered much, because podcasting tended to be almost exclusively for the young, geeky or both. Last week, however, that changed.

That is because Apple, which dominates the online-music business, has integrated the requisite "podcatching" software into the latest release of iTunes, the jukebox software that accompanies the iPod. Finding and subscribing to podcasts, once a fiddly business, is now simple. One click takes users to a page of podcasts on offer, from public-radio shows to the eccentric ramblings of geeks; another click sets up the subscription. Podcasts are transferred to an iPod automatically when it is plugged in. So the iPod has finally staked its claim to a medium that already bears its name.

This could have significant consequences. "Something remarkable is happening here," beams a voice in one of this week's podcasts by Adam Curry, a former MTV host who pioneered the medium last year. "Radio is springing free of the regulated gatekeepers who've managed what you can hear since radio was invented. It's jumping into the hands of anyone at all with something or nothing to say." Indeed, novices will soon discover that many podcasts—like their close relatives in the text world, blogs—really do have astonishingly little to say. But a creative lid has come off.

Musicians and pundits who have no hope of ever making it on to commercial radio can now build their own audiences. For listeners too, the change may be dramatic. Traditional broadcast radio, says J.C. Herz, a pop-culture expert, is "a numbingly predictable heavy-rotation formula with too much blather and too many ads". The only reason people put up with it, she says, is the lack of alternatives. Podcasting is one alternative that promises to upend the trend in recent decades towards dumber, duller radio. But there are others, too. Over 35m American households—about half of those with broadband internet access—listen to online radio stations, according to Forrester, a technology consultancy. And some 7m Americans subscribe to ad-free satellite radio. Increasingly, satellite receivers are pre-installed in new cars, so that number should reach 20m by 2010, reckons Forrester. Its forecast for podcast listeners by 2010 is 12m American households. That estimate, however, was made before Apple stepped in.

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The Baugur affair

In hot water

Jul 7th 2005
From The Economist print edition

One of Iceland's tycoons faces criminal charges. All politics, he says

DID Jon Asgeir Johannesson, an Icelandic multimillionaire, really defraud his family firm, Baugur, while it was listed on Iceland's stock exchange? Yes, say the police, who charged him on July 1st. No, says Mr Johannesson, Baugur's chief executive; this is a political fight, and the former associate whose accusations put the police on to the case is just out for revenge. No, says Baugur, the alleged victim—which, taken private in 2003, is 68% owned by Gaumur, the family's holding company.

Though police interest has been public knowledge since 2002, the charges—there are more, tax evasion included—have rocked the small but hugely ambitious world of Icelandic business. Their repercussions spread far beyond Iceland.

In all, six people face 40 charges, including Mr Johannesson; his father, founder of the group; and his sister Kristin, chief executive of Gaumur. Just who—allegedly—did what is unclear: few details are yet public.

Baugur's retailing activities spread wide. It owns Hagar, mostly in Iceland and Sweden. Last autumn it bought Denmark's Magasin du Nord department-store group. But its big expansion has been in Britain.

In 2002 it joined with a controversial British tycoon, Philip Green, to buy Arcadia, a fashion retail group. After a police raid on its Icelandic headquarters, Baugur sold him its stake (whose purchase features prominently in the charges), bought some minor retailers and went after supermarkets. It first bought a stake in Britain's troubled Big Food group—whose stores, appropriately, are branded “Iceland”—then formed a consortium that took it over. This year it has tried the same tactic on Somerfield, another struggling supermarket group, though the charges have jeopardised its role in the plan. Rumours recently suggested a grander, yet also troubled, target, Marks & Spencer.

At home, the affair extends well beyond retailing. Baugur is also big in media. Last year, the then prime minister, David Oddsson (who once claimed that Baugur tried to bribe him) pushed through a media law aimed at limiting Baugur's interests. But it was blocked with a veto—the first in Iceland's history—from the country's president, whose daughter, Mr Oddsson noted, works for Baugur.

Banking, too, may be affected, and not only by Baugur's closeness to Kaupthing, Iceland's biggest bank, which at one time owned a 22% stake in Baugur. This sector has recently been mired in controversy, set off by reports in one of the Baugur newspapers questioning how the past Oddsson government privatised state banks over several years up to 2003.

Meanwhile, the bosses of ex-state Landsbanki—a wealthy dynasty, close to Mr Oddsson's party, whose business empire now spans pharmaceuticals, telecoms and financial services, having started in Russian brewing—have been extending their influence in Islandsbanki, the third of the big three. Hardly had they bought an extra 4% of it than two rival entrepreneurs bought 5%. One of them was Mr Johannesson. So the charges spread into media and banking, and on into politics. Or is that, as he claims, where they began?

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Business in Indonesia

Foreigners welcome

Jul 7th 2005 | JAKARTA
From The Economist print edition

Foreign firms are doing more business in Indonesia, perhaps unwisely

WHEN Susilo Bambang Yudhoyono became president of Indonesia last year, he vowed to make the country a place where foreigners could do business. As proof of his intent, he promised to resolve three long-running disputes with foreign investors within 100 days of taking office. Yet the disputes still fester.

The three spats exemplify the capriciousness of doing business in Indonesia. ExxonMobil's local operation wants to extend its contract to exploit the Cepu oil field. Since 2001, successive governments have procrastinated over the extension. Recently, several parliamentarians announced that if Mr Yudhoyono's team ever reached a deal, they would block it anyway. Meanwhile, the authorities are not letting Cemex, a Mexican cement-maker, exercise an option to buy the government's stake in Semen Gresik, a local cement firm, because of opposition from managers, workers and politicians. And the government refuses to pay a $261m arbitration award to Karaha Bodas, an energy firm whose contract to build a geothermal power plant it suspended in 1998.

True, there have been hints of progress of late. The government recently said that it had agreed the rough contours of a deal with ExxonMobil over Cepu and hopes to sign a formal contract soon. Officials say they are still trying to negotiate settlements with Cemex and Karaha Bodas.

More broadly, the government has launched a vigorous anti-corruption campaign. So far, a provincial governor, an election commissioner and the head of a partially state-owned bank, among others, have been investigated. Mr Yudhoyono has visited the customs department, police headquarters and attorney-general's office to stress the need for transparency and efficiency. Revisions of the investment, tax and labour laws are in the works.

Foreign businessmen have been impressed, if the latest investment figures are anything to go by. Approvals for foreign direct investment reached almost $5 billion in the first four months of the year, 50% up on the same period last year. In May, Indonesia saw its biggest foreign takeover to date, Altria's purchase of Sampoerna, a clove-cigarette-maker, for $5 billion.

That is despite there remaining plenty of evidence that the authorities are still inclined to behave in an arbitrary and unpredictable manner. Ministers contradict each other and announce things that come as a surprise to the firms they affect. Abu Rizal Bakrie, chief economics minister, said in May that Cemex had agreed to sell its stake in Semen Gresik and to invest instead in facilities of its own in Indonesia—a scenario that Cemex pointedly refuses to confirm.

Above all, the government shows no sign of trying to handle the cases in a principled, consistent manner. Even if, as Vice-president Jusuf Kalla blithely insists, fixes can be found for the three test cases, that will do nothing to reassure investors about the government's respect for the rule of law. The idea of simply honouring the contracts with Karaha Bodas and Cemex—or even justifying their abrogation—does not seem to be on the agenda at all.

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French privatisation

In name only?

Jul 7th 2005 | PARIS
From The Economist print edition

The sale of shares in Gaz de France will raise money without changing control

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SOME 60 years after the nationalisation of France's gas and electricity industry, Dominique de Villepin, the country's new prime minister, is selling off a chunk of Gaz de France (GDF), the former gas monopoly. When the shares started to trade on July 8th, they were expected to fetch up to €4.9 billion ($6 billion)—the world's biggest initial public offering (IPO) so far this year. All being well, Mr de Villepin plans a far bigger sale, in October, of shares in mighty Electricité de France (EDF).

As always in France, the sale has been fiercely opposed by trade unions. Workers at both GDF and EDF are bastions of the Confédération Générale du Travail, the Communist Party's union. Last year, they took to the streets and caused some 800 blackouts across the country. In May, after French voters rejected the proposed European Union (EU) constitution, the unions called for the GDF and EDF sales to be scrapped because, they said, the vote was a message to leave public services intact. Accepting that GDF was lost, they then formed an association for the firm's *citoyens actionnaires* ("citizen shareholders"). Its goal, they say, is to protect GDF as a public company that serves the general interest, to defend it against its managers' attempt to turn it into "a company like all the others" and against capitalists' demands for "ever bigger profitability".

Mr de Villepin resisted union pressure because he faces even greater financial and political pressures. On July 6th *Le Monde* reported that, according to a confidential study by the treasury, France will continue to breach the rules of the EU's stability pact despite pledges to bring its deficit and debts within the pact's limits this year. Without the expected proceeds from privatisation, the state coffers would be even deeper in the red.

But, as is often the case in France, these privatisations will not get the state out of the business. The government is keeping 80% of GDF—the largest government stake in any listed utility in Europe. In a recent report, the OECD criticised France for maintaining its position as the dominant shareholder in too many privatised firms—with competition suffering in energy, telecoms and transport as a consequence. For instance, the government kept 32% of France Telecom, 30% of Thales, a defence company, 18% of Air France, the national airline, and 15% of Renault, a carmaker.

None of which has stopped investors rushing to buy GDF shares. The IPO has been over-subscribed, with strong demand from individual investors. GDF's boss, Jean-François Cirelli, has big plans, including spending €17.5 billion in the next three years on greenfield projects and buying gas-distribution companies in Europe. But investors may be more tempted by his promise to double GDF's dividend by 2007 and maybe to return even more money to shareholders. That is a promise the state, with its financial woes and controlling stake, is likely to hold him to.

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Internet politics

Eminent domain

Jul 7th 2005
From The Economist print edition

In a pre-emptive strike, America decides to keep control of the internet

AMERICA created the internet. It also controls the key physical infrastructure that makes it work. For years, some other governments have wanted more say and have lobbied to put the internet under the auspices of the United Nations (UN). America's government seemed willing to give up its governance role, but planned to pass the reins to an industry self-regulatory group it set up. This plan did not satisfy those governments that wanted UN oversight.

On June 30th, the Bush administration brought matters to a head by announcing, unexpectedly, that after all it will retain its authority over the Internet Corporation for Assigned Names and Numbers (ICANN). This manages the internet's domain-name system of addresses, such as .com, and the underlying internet protocol numbers. This system—which runs on computers almost entirely in America—is critical to the smooth operation of the network. Many governments are apoplectic at what they see as yet another example of American unilateralism and plan to denounce it at ICANN's board meeting in Luxembourg on July 11th-15th.

America said it took this step to ensure the internet's “security and stability”. The main danger, in its view, was that other governments would muck it up. The policy was surely a pre-emptive strike against proposals from the UN's Working Group on Internet Governance, due in mid-July, most of which favour inter-governmental oversight of the domain-name system, preferably under the UN. “No single government should have a pre-eminent role in relation to international internet governance,” says a draft of the report obtained by *The Economist*.

Among the main supporters of UN oversight are some countries troubled by the globalising forces unleashed by the internet—such as China, Cuba, Saudi Arabia and Syria. America decided that the best way to keep the internet free from sinister political interference was for it to retain control. That may seem paradoxical, but businesses, at least, seem delighted. This week, the International Chamber of Commerce issued a statement urging the International Telecommunication Union, a UN agency, to keep its hands off the internet.

In theory, there is no reason why ICANN's monopoly on net names should be forever sacrosanct. Nothing prevents the creation of new naming systems alongside ICANN-sanctioned domains. Any country that dislikes American oversight is free to develop an alternative system with addresses it controls. Maybe that competitive pressure would even keep the American internet up to scratch.

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Face value

Movies to go

Jul 7th 2005
From The Economist print edition

Can Netflix's Reed Hastings succeed in the battle to deliver movies online?

LATER this year, Netflix will launch a new service for downloading movies from the internet. “It will be underwhelming,” promises Reed Hastings, chief executive of America's leading online DVD-rental company. Despite a recent ruling by America's Supreme Court that gives entertainment companies more ammunition to fight against illegal file-sharing, movie studios are likely to remain extremely cautious about what films they make available for a fee on the web.

For now, that suits Netflix. Mr Hastings believes that the humble DVD—and, eventually, high-definition versions of it—will remain popular for some time, not least because that is what the movie industry wants: sales of DVDs and fees from rentals are an essential source of the studios' profits from new releases. But Mr Hastings is also betting that by the time movie-download technology becomes more mature and online titles more widely available, his subscriber base for DVD rentals will be big enough to put Netflix in a strong position to prosper in the online marketplace—where he is likely to face new competitors such as Yahoo!, Microsoft, the studios themselves and, no doubt, many start-up firms offering rival download services.

Changes in technology encourage start-ups with innovative ideas to enter markets, just as Netflix did in 1999 when—having been stung with a $40 late-payment from a Blockbuster video-rental store—Mr Hastings launched its subscription service. He was already a successful entrepreneur, having built up a software company before he started Netflix. For its most popular service, Netflix charges users $17.99 a month for an unlimited number of DVD rentals. Titles are ordered via the company's website and dispatched overnight. Customers mail them back in a pre-paid envelope, which releases the next movie on a personalised list of films to see. Subscribers can have up to three DVDs out at any time. Needless to say, there are no late fees.

The Netflix business model has proved to be such a simple and highly effective combination of the online and offline worlds that it has spawned imitators in Britain, France, Germany, Australia and Japan. Netflix, which is based in Los Gatos, California, was about to launch in Britain last year when it decided it had better withdraw from going international, for now, in order to concentrate on a life-threatening war on its home front. The all-conquering retailer, Wal-Mart, and Blockbuster, the world's biggest chain of video-rental shops, both decided to offer online DVD rental at lower prices. Amazon has since started to experiment with a DVD-rental service in Britain—but has not yet launched a similar service in America, and some suspect it may instead team up with an existing competitor.

Certainly, the cost of entering the market has gone up. Netflix has slashed its own prices and launched a one DVD out at a time service for just $9.99 a month. In the past year its share price tumbled as investors saw profits being pumped into an aggressive marketing campaign (costing nearly 20% of its revenues). The company expects to make a net loss of $5m-15m this year. Nevertheless, Mr Hastings says Netflix has $175m in cash and no debt. “We can sustain this for a very long time,” he adds. Indeed, Netflix is showing signs that it is getting the upper hand. In May, Wal-Mart pulled out, awarding its online DVD-rental business to Netflix. Yet, tempting as it might be, Mr Hastings declines to trumpet that Netflix beat the world's biggest retailer. Indeed, Wal-Mart's bosses say they merely took a strategic decision to focus on selling DVDs rather than renting them. Netflix and Wal-Mart will now promote each other's products.

Meanwhile, Blockbuster, which lost $1.2 billion last year, hopes to win 2m customers by next spring for its online DVD-rental service, which costs $14.99 a month for the standard package. But Netflix has already seen its number of subscribers grow to 3m and it expects to reach 4m by the end of this year. And there has been something of a rebellion by some Blockbuster shareholders, which resulted in Carl Icahn, a well-known corporate raider, winning a seat on the board. Blockbuster has been testing out higher fees, which suggests that Mr Icahn's priority could be stemming losses, not undercutting Netflix.

War of the worlds

Why are people prepared to pay more to use Netflix—the movie they get, after all, is exactly the same? Attention to customer needs and quality of service is Mr Hasting's answer. Indeed, Netflix was recently ranked by ForeSee Results, a market-research firm, as the top internet retailer by customer satisfaction. But something else is becoming increasingly important in e-commerce: the ability to amass an inventory that goes far beyond what any high street operation can hope to sustain.

Netflix has what some people fashionably call a “long tail” business. Its catalogue of more than 45,000 titles means that it can cater to almost any interest. Such a depth of movie offerings, plus online features such as movie reviews and recommendations, increases its popularity. Unlike a typical high street video-rental store, which might get the bulk of its revenue from just a few hundred recent titles, Netflix's revenue comes from a far broader selection: some 35,000 different film titles are contained in the 1m DVDs it sends out every day.

Netflix uses 35 distribution centres within metropolitan markets to help it meet its aim of overnight delivery. Yet when online delivery of movies, in whatever form it takes, eventually starts to take off, that legacy infrastructure will count for nothing: warehouses will be replaced by huge computer servers that can be based anywhere. This will not happen overnight, however. And in the transition “we can do mixed mode,” says Mr Hastings. If a movie is not available for download—as many classics may not be for some time—then Netflix can still pop a DVD version into the old-fashioned mail.

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Nuclear power

The shape of things to come?

Jul 7th 2005
From The Economist print edition

Alamy

Climate change is helping a revival of the nuclear industry, though its economics still look dodgy

Get article background

THINGS have not gone well for the nuclear industry over the past quarter century or so. First came the Three Mile Island accident in America in 1979, then the disaster at the Chernobyl plant in Ukraine in 1986. In Japan, Tokyo Electric Power, the world's largest private electricity company, shut its 17 nuclear reactors after it was caught falsifying safety records to hide cracks at some of its plants in 2002. And the attacks on September 11th 2001 were a sharp reminder that the risks of nuclear power generation were not only those inherent in the technology.

Nor was safety the only worry: there were financial problems too. British Energy, Britain's nuclear-energy operator, required successive government bail-outs. Britain also recently finalised a £50 billion ($90 billion) scheme to deal with the nuclear-waste liabilities of British Nuclear Fuels (BNFL), an inept re-processor of nuclear waste that is itself bust.

But lately, things have brightened for the nuclear industry. In Asia, which never turned against it in the way the West did, the prospects are excellent. China already has nine nuclear reactors, and is planning to commission a further 30. New capacity is being built or considered in India, Japan, Taiwan and South Korea. Russia has several plants under construction.

Now western governments are increasingly looking anew at nuclear energy. A few weeks ago TVO, a Finnish consortium, started work on the first new nuclear plant to be built on either side of the Atlantic in a decade. Pertti Simola, TVO's chief executive, proclaims that, “Finland has opened the door to a new nuclear era! Many western countries will come behind us.”

France's parliament has recently given its approval for a new nuclear plant. Guillaume Dureau of Areva, the world's largest nuclear supplier, captures the dizzy mood that has overtaken vendors: “We are pretty convinced of a nuclear revival and [we] need to prepare for it. We need to hire 1,000 engineers.”

Despite its earlier doldrums, the nuclear industry is still a sizeable business. In 2004 Areva had sales of €6.6 billion ($8.2 billion). That figure includes mining uranium, designing power plants and reprocessing waste fuel. General Electric's nuclear division, which designs and builds plants but does not handle fuel

or waste, turned over about $1.1 billion last year (its turnover was double that figure if sales of non-nuclear bits of nuclear plants, such as generators and turbines, are included). Westinghouse, an American brand currently owned by BNFL, which recently put it up for sale, had sales of around £1.1 billion ($2 billion).

The main reason for the shift is climate change. As it has risen up the political agenda, so the impetus for a nuclear revival has grown.

More, and more respected, voices have been making the case that nuclear energy is essential if the rate of change is to be slowed. As a result, there is an unlikely alliance between the nuclear industry and many environmentalists, as a growing number of greens have come to believe that nuclear energy is the best way to reduce carbon emissions. Industry lobbyists are finding support from unexpected areas. Keith Parker of the Nuclear Industry Association, a British trade group, points to a recent quote from James Lovelock, a founder of Greenpeace: “Only nuclear power can halt global warming.”

Scientists are also lending their support. Sir David King, Tony Blair's chief scientist, recently argued that one further generation of nuclear power stations is needed (in Britain at least) to buy time, in order to keep down emissions of carbon dioxide, the chief greenhouse gas, while new carbon-free non-nuclear technologies are developed. He thinks that renewable sources of energy are not currently up to the task: “We need another generation of nuclear-fission stations.” Others agree. The World Nuclear Association, an industry body, dismisses its green rivals in a recent report: “the potential scope for renewables contributing to the electricity supply is very much less because the sources, particularly solar and wind, are diffuse, intermittent and unreliable.”

Such opinions have caused consternation among nuclear energy's long-standing opponents, notably Europe's green movement. Anti-nuclear sentiment was so strong in Germany at the end of the 1990s that the ruling socialist-green alliance banned new plants. Sweden was the first country to turn against nuclear plants, in a referendum back in 1980; at the end of May it shut down its second nuclear plant. Yet in both countries opinion polls suggest waning public opposition to the nuclear option. Indeed, Germany's Christian Democrats now say they may overturn the ban if they win the forthcoming national election. In Finland, says TVO's Mr Simola, concern about climate change was the chief reason why his country pushed ahead with the new power plant.

In America, although the Bush administration remains hostile to any mandatory action on slowing global warming, it is keen to boost nuclear power. That has led some greens to take the view that a nuclear revival is better than doing nothing much about climate change. Leaders of respected environmental outfits such as Environmental Defence and the World Resources Institute have recently made positive noises about nuclear power as part of a response to global warming.

Of course, nuclear power is not the only carbon emission-free option. Making existing energy production more efficient, and reducing waste in the use of energy by consumers, would have a big economic and environmental impact. Renewable energy sources such as wind and waves have plenty of backers.

There are also direct rivals to new nuclear plants, such as fossil-fuel plants with carbon sequestration that can provide baseload power. A flurry of investment and experimentation, from Algeria to China to America, is already under way in this area.

Vattenfall, a Swedish nuclear utility, is investing in technology to remove carbon from its newish coal plants in eastern Germany and Poland. Cinergy, an American utility just bought by Duke, is looking into coal gasification and carbon sequestration in Indiana. A Scottish consortium led by BP recently announced the first commercial-scale project to produce carbon-free power from natural gas, re-injecting the waste carbon dioxide into fields in the North Sea—thus not only storing the gas underground, but also enhancing hydrocarbon recovery from the field. And combined heat and power, which allows companies and householders to use the heat created by power generation as well as the electricity it produces, is booming. But the nuclear industry has the momentum right now. That's partly because its economics have improved markedly.

Better management allows companies to make existing plants much more efficient. In America, for instance, the country's 103 nuclear plants are no longer owned by individual municipalities. “Nuclear consolidators are the key,” argues Michael Wallace of Constellation Energy, a utility that owns several plants and hence can retain good managers, share best practices, gain economies in maintaining parts and inventories and so on. The top ten nuclear firms now own 61% of the sector. Exelon, the largest firm, has a 15% share. American nuclear power plants' capacity utilisation has risen from 56% in 1984 to more than 90% today.

This is a lesson that France had already learned, says Bernard Dupraz of Electricité de France. EDF is responsible for all the country's nuclear plants. Unlike America, where no two nuclear plants are exactly alike, France stuck with a few standard designs. “We standardised nuclear plants like Ford did the Model T.” The results: 20% lower operating costs and 30-40% lower capital costs than those of one-off designs used elsewhere, notably in Britain.

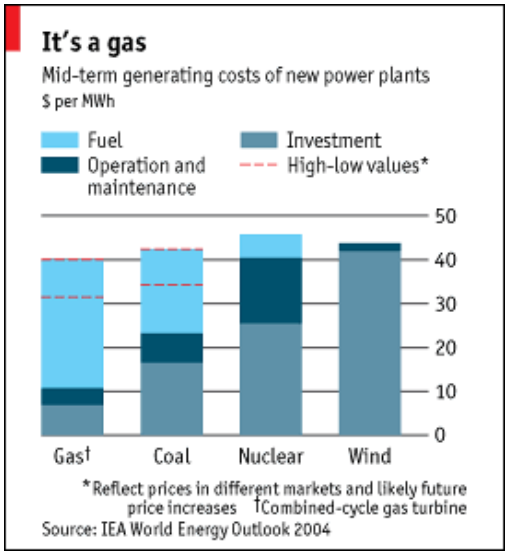
CERA, a consultancy, calculates that 31 countries have commercial nuclear-power reactors today. Taken together, these 439 reactors produce about 16% of the world's electricity, worth annually $100 billion-125 billion. And the pot is growing.

Expansion in China alone is likely to involve some $50 billion or more of capital spending. That's quite a prize—though it is important to put China's nuclear interest into perspective. Even if it really builds all 30 mooted plants, nuclear power will still make up only about 5% of its electricity mix in 2030. Meanwhile, natural gas is expected to grow from a 1% share today to over 6%, according to the International Energy Agency (IEA).

In many power markets today, nuclear electricity is the cheapest you can buy. Entergy's deregulated nuclear plants produced 13% of its revenues but a quarter of its profits last year. It costs German utilities perhaps 1.5 (American) cents per kW-hour to make nuclear electricity, estimates Vincent Gilles of UBS, an investment bank, but they can sell it for three times that amount once credits from Europe's carbon-trading scheme are included. In contrast, it costs 3.1-3.8 cents to produce power from natural gas in Germany and 3.8-4.4 cents to produce it from coal. In America, where there is no mandatory carbon regulation (and hence no penalty on fossil fuels), nuclear power has less of an edge: coal power costs about 2 cents per kW-hour on average today, gas-fired power costs about 5.7 cents, while nuclear cranks out electricity at 1.7 cents or so.

But the economic case is not as clear-cut as it seems. The costs of nuclear power produced by existing plants are likely to be far lower than the costs of newly built plants, because the capital costs of nuclear plants—typically reflecting half to two-thirds the value of the project in present-value terms—are long forgotten. Most of today's plants were built in an era when central planners or state utility boards had no idea of the true cost of capital. Today's low interest rates are good for big capital projects like nuclear, but those rates may change sharply in the future. At the same time, gas and oil prices—whose current astronomical levels enhance nuclear's charms—may well fall.

Subsidy, what subsidy?



Critics also argue that the best designs the nuclear industry can come up with are not competitive with rival energy technologies in the open market. The nuclear industry points to some studies that seem to suggest that nuclear plants might be economic if only their “life cycle” benefits (such as lack of greenhouse gases) and their rivals' disadvantages (such as fuel costs for natural gas plants) are factored in.

For example, the Nuclear Energy Agency, an arm of the OECD, has just released a study done jointly with the International Energy Agency (IEA). After reviewing the economics, it seems to conclude that

there is indeed a bright future for nuclear: “on a global scale, there is room and need for all baseload technologies.” Assuming a discount rate of 5%, it argues that the cost of generating power from new nuclear plants would cost between $21/MW-hour and $31/MW-hour; costs for gas-fired power, it reckons, would range from $37/MW-hour to $60/MW-hour. (The report also assumes high gas prices, which favour nuclear, a view contradicted by the IEA's official forecast of a medium-term reduction in gas prices.)

But there's plenty of scope for argument about the economics of nuclear power generation, because they are so sensitive to assumptions about the cost of power from other sources. As Ed Cummins of Westinghouse insists, “The biggest motivator for nuclear today is $6 [the price per MBtu] natural gas. If gas goes back to $3.50, then nuclear plants aren't competitive.”

The other source of uncertainty is the disposal of radioactive waste. That's what messed up the economics of Britain's nuclear programme: Britain decided to reprocess its waste, which proved hugely expensive. America, by contrast, just stuck it in swimming pools—literally—at the power plants. The current consensus is that the best solution is geological storage—that is, to bury the waste very deep. The bad news is that nobody is making much progress getting there, or knows how much it will all cost in the end.

Taking into account the uncertainties, most studies done on nuclear economics (including the most authoritative ones, done by the Massachusetts Institute of Technology and by Britain's Royal Institute of International Affairs) conclude that new plants built by the private sector, with investors bearing the full brunt of risks, are not economic without subsidy.

Though nuclear vendors are promising that their new designs will cost only $1,500 per kW of installed capacity, that assumes ideal conditions and no delays. A more realistic assessment (indeed, the consensus view among experts not aligned with the nuclear industry) is that new plants will probably cost close to $2,000 per kW. That may be less in real terms than the capital cost of previous generations of nuclear plants, but it is still about double the capital cost of a conventional coal plant today. The upshot of all this is that even today's cheaper, safer nuclear designs are still more expensive than coal or gas.

The money men are not very enthusiastic. Standard & Poor's, a rating agency, recently declared, “The industry's legacy of cost growth, technological problems, cumbersome political and regulatory oversight, and the newer risks brought about by competition and terrorism may keep credit risk too high for even (federal legislation that provides loan guarantees) to overcome.”

Part of the problem is that nuclear plants are seen as too “lumpy” and uncertain as investments. A 1,000MW nuclear plant would cost $2 billion and take at least five years to build. A coal plant of that size would cost perhaps $1.2 billion and take three to four years, while a combined-cycle gas plant that size costs about $500m and takes less than two years to get up and running. The bigger the project, the more susceptible it is to delays—and UBS's Mr Gilles estimates that a two-year delay in nuclear projects wipes out 20-25% of the project's value to investors.

Political risk is a problem, too. The links between nuclear power and weapons hurt the business—as was sharply illustrated last week. Westinghouse was in the bidding against French and Russian companies for a Chinese contract. But the House of Representatives, fearful of giving China access to American nuclear know-how, voted down a $5 billion loan from America's Export-Import Bank.

So, if the economics are so unpromising, why is so much nuclear capacity being built? Some of it—in China, for instance—may be the result of mixed motives. China could be after the technology that America wants to deny it. Security might also be a factor: energy importers may want a proportion of their needs met by sources over which they have control.

Nuclear fans point to Finland where a private consortium seems to have managed to finance a new power plant without government subsidy. But was it done without subsidies or unfair state aid? Absolutely, insists TVO's Mr Simola. “You must be joking,” retorts UBS's Mr Gilles.

In fact, the answer is unclear. TVO is a consortium involving six shareholders—but one of them is a state-owned utility, Fortum. TVO's owners are also its only customers. Some of those customers are big paper and pulp companies, who use a lot of power; others are municipalities, which may not be sensitive to market economics. Indeed, the €3 billion deal is not a conventional commercial transaction. Mr Simola explains that there is a lifetime power-purchase contract agreed at zero profit: “We pay dividends in the form of competitive power,” he jokes.

The plant is to be built by France's Areva on a fixed-price bid. If there are delays or massive cost overruns, Areva must cover them. Areva's Mr Dureau vigorously denies that French government ownership means that that country's taxpayers will be subsidising Finnish power: his firm will yield all its assets and go bust before the French taxpayer will pay a penny, he insists. But if it does go bust, the French taxpayer must write that cheque to TVO.

Even if the Finnish experiment is not explicitly subsidised, the model may nevertheless be tricky to replicate elsewhere. If it can be—and there is some interest in France and America among heavy energy users—then the nuclear industry may yet be justified in claiming that new nuclear plants can be built without state aid.

Yet most studies reckon that even a moderate carbon tax would not make nuclear power generation competitive in a free energy market. Europe's emissions-trading system (ETS) is, in effect, that sort of a tax. And according to Oxera, a British consultancy, even with that implicit tax on carbon-based power generation, new nuclear plants would not be economic without government help.

But if the implicit tax rose, that might change. The point of a carbon tax is to reflect the cost to society of damage that using carbon does. Setting a price on those social costs is difficult. Europe's ETS implies that the social costs of carbon dioxide are €20 per tonne; but a British government study in 2002 estimated them at £70 (€112). Such estimates are necessarily vague; but if that higher figure is fed into Oxera's model, new nuclear plants begin to look economically viable.

However, politics make it unlikely that carbon is going to pay its full social costs—for some time to come. That's why some governments—including America's—are thinking of subsidising nuclear instead.

President Bush is trying to shoehorn a provision into his energy bill that would give the nuclear industry about $500m in insurance against the risk of regulatory delays, and a further $6 billion or so in subsidies now being considered for new nuclear plants. American utilities want several billion dollars for the engineering and construction costs associated with building the first three or four such plants. They are also hoping for over $500m in subsidies to go through the licensing process, and an extension of the government's blanket insurance policy against catastrophic accidents.

They may get them. There's a powerful business lobby in America that's hostile to the idea of importing emissions trading from Europe. Subsidising nuclear is one of the only ways of squaring that lobby's interests with the electorate's rising awareness of the need to do something about climate change. With President Bush and the tree-huggers both on its side, the nuclear industry is back in the game.

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Saving by companies

The corporate savings glut

Jul 7th 2005
From The Economist print edition

Companies, not emerging economies, are leading the global shift to thrift

THE anti-globalisation protesters at this week's G8 summit have long argued that companies make too much money. As it happens, economists also think that firms have “excess profits”—although not in the sense that the protesters would recognise. Basically, managers don't know what to do with their cash. For the past three years, while profits have surged around the globe, capital spending has remained relatively weak. As a result, companies in aggregate have become net savers on a huge scale. Their thrift may explain why bond yields are now so low.

Not that there is any shortage of explanations on offer for why real bond yields have fallen in recent years. Some people suggest that they reflect expectations of a slowdown in growth, or a lower inflation-risk premium or, perhaps, pension funds' increased appetite for fixed-income assets. But the theory that is currently all the rage holds that yields have been depressed by a global savings glut.

Ben Bernanke, a former governor of America's Federal Reserve who is now chairman of George Bush's Council of Economic Advisers, argued earlier this year that excess saving by emerging economies was to blame for both America's large current-account deficit and lower bond yields. Following a series of financial crises, these economies slashed investment and swung from a combined current-account deficit of $93 billion in 1996 to a surplus of $336 billion last year. Since bond yields should reflect the demand and supply for funds, this increase in net saving could indeed have reduced yields. However, a new study by economists at J.P. Morgan concludes that in recent years an increase in saving by companies in developed countries has been far more important than emerging economies' thrift.

Over half of emerging economies' huge swing from external deficit to surplus had occurred by 2000. However, American bond yields were roughly the same in that year as in 1996; the big decline in yields is more recent. Since 2000, the corporate sector has stood out. Companies in the main developed economies have switched, as a group, from being big borrowers to being net savers: ie, their profits exceed their capital spending. The total increase in companies' net saving in the past four years has been more than $1 trillion, 3% of annual global GDP and five times the increase in net saving by emerging economies over the same period. J.P. Morgan estimates that about half of the gap between the current real yield on American ten-year Treasury bonds and its average since 1960 is due to this increased corporate saving.

It is striking how similar companies' behaviour has been despite big differences in countries' growth rates. The economies of America and Britain have boomed, while those of Japan and the euro area have stalled, yet in all of them firms are now running a financial surplus, using their spare money to repay debts, buy back shares or build up cash. This is odd, because normally companies are net borrowers, investing to boost future output and incomes, while households as a group are net savers, providing firms with the capital to invest.

Firms have been net savers for the odd year in the past, but a run of several years is highly unusual. Since 2002 American firms have had an average net financial surplus of 1.7% of GDP, compared with an average deficit of 1.2% of GDP in the previous two decades (see chart). Corporate Japan has run an average surplus over the past three years of no less than 6.2% of GDP, compared with an average deficit of 2.3% in the 1980s and 1990s. In fact Japanese firms have been in financial surplus since 1994, desperately trying to reduce the debts they built up during the bubble economy in the late 1980s. Corporate cost-cutting—in both capital spending and new hiring—has been a persistent drag on Japan's growth rate. The good news is that corporate debt as a percentage of GDP has fallen to the level of the mid-1980s, before the bubble really inflated.

Now American and European firms seem to be following in the footsteps of the Japanese, having been forced to cut back on borrowing after a binge in the late 1990s. It is also worth noting that a large chunk of the rise in corporate saving in America in recent years has come from the financial sector, where profits have soared.

The recent increase in corporate saving in the euro area has been more modest than in America or Britain, but it has made a bigger dent in growth, because the single-currency zone, unlike the other two economies, has not been cushioned by either an increase in government borrowing or a fall in saving by households.

Hey, big saver

Alan Greenspan, chairman of the Federal Reserve, has called the fall in bond yields while short-term interest rates are rising a “conundrum”. In light of the increase in corporate saving, says Chris Watling of Longview Economics, a consultancy, the real conundrum is not that bond yields are so low, but that firms are saving and not investing when profits are strong and money is cheap. If it is because of over-investment in the bubble years of the late 1990s, then investment should recover and bond yields rise, once balance sheets have been repaired and spare capacity has been used up. Mr Watling points to some tentative signs that firms are starting to borrow and invest again as evidence that this is happening: in America, bank lending to firms is now growing faster than consumer lending for the first time since the late 1990s. J.P. Morgan agrees that companies' behaviour should return to normal relatively soon, and therefore predicts that the yield on ten-year Treasuries will rise from 4% to 5% by the end of 2005.

In contrast, the economics team at HSBC expects corporate investment to remain weak. Japanese firms' decade-long efforts to repay debt provide a sobering lesson. America's pick-up in investment last year may have been spurred by accelerated depreciation allowances which have merely encouraged companies to bring forward spending from future years. If company bosses recognise that the current

consumer boom is built on shaky foundations—in particular, rising house prices—they are likely to be reluctant to invest. If firms continue to save and consumer spending slows, as house prices level off or even decline, then weaker growth will lie ahead. Could it be time, perhaps, to dust off the works of Keynes, and swot up on the “paradox of thrift”?

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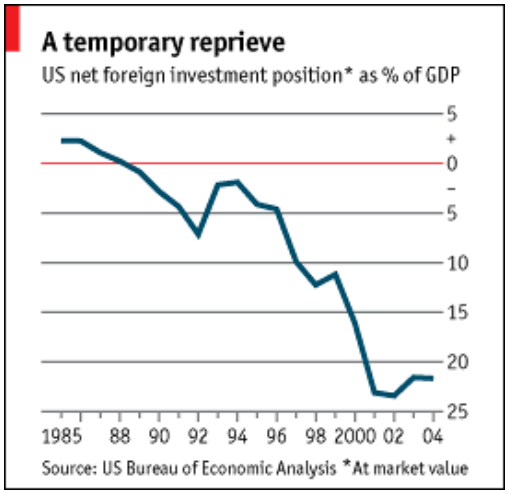
America's foreign debt

Show me the money

Jul 7th 2005
From The Economist print edition

Mysterious happenings in America's international financial accounts

AT THE start of this year, when the American dollar stood at $1.36 to the euro, most economists expected it to stay weak or to become still more feeble. Instead it has since risen by 14% against Europe's single currency, hitting a 14-month high of $1.19 this week. Another puzzle: contrary to dire predictions that America's vast current-account deficit would plunge the country ever deeper into debt to foreigners, recent figures show that foreign debt has actually fallen, relative to GDP, in the past few years. Does this mean that the current-account deficit isn't a problem after all, and that the dollar will keep on climbing? No, it doesn't.



Last year, America had a current-account deficit of $668 billion. In effect, it had to borrow this amount from the rest of the world. However, the new numbers, published last week by the government's Bureau of Economic Analysis, show that America's net external liabilities rose by only $170 billion in 2004, to $2.5 trillion. The mystery goes deeper. Since the end of 2001, America's cumulative current-account deficit has amounted to $1.7 trillion, yet America's net external liabilities have increased by only $200 billion, and have fallen as a percentage of GDP (see chart). What's going on?

The explanation is that the value of foreign assets and liabilities changes with exchange rates and share prices. The rally in global stockmarkets in 2004 boosted the value of America's external assets by more than the value of its liabilities because Americans own more shares abroad than foreigners own in the United States. In addition, foreign stockmarkets outperformed Wall Street last year.

Even more important over the past three years has been the impact of a cheaper dollar. About 70% of America's assets abroad are denominated in foreign currencies, so when the greenback falls, their dollar value rises. Meanwhile, as the home of the world's main reserve currency, America has the advantage that virtually all of its foreign liabilities are in dollars, so that the currency's depreciation does not increase their value. Thus a fall in the dollar boosts America's net wealth.

It may be tempting to conclude that America can comfortably continue to run huge deficits and let a falling dollar erode the real value of its external debt. But foreign investors are not stupid: if they expected a persistent decline in the dollar, they would demand a higher yield on American assets to compensate them for their expected loss. This would increase the current-account deficit.

If the dollar hangs on to its gains, then the end-2005 figures for America's net foreign indebtedness could prove truly shocking. Brad Setser, of Roubini Global Economics, a research firm, estimates that at current exchange rates the capital loss on America's foreign assets could amount to $350 billion this year. Add that to his forecast for the current-account deficit of $820 billion, and it seems that America's net foreign liabilities could leap by $1.2 trillion, to $3.7 trillion by the end of 2005. Of course, a further drop in the dollar and a fall in American share prices could trim those liabilities again in 2006. But that is hardly a reason to buy dollars.

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Morgan Stanley

The day after

Jul 7th 2005 | NEW YORK
From The Economist print edition

Feted on his return to his troubled old firm, John Mack must justify the hype

AP

Back in town

GREAT timing. John Mack returned to Morgan Stanley, as chief executive, just before the July 4th weekend, one of the few holidays that Americans take seriously. That ensured at least a one-day honeymoon. It may not last much longer. In short order, Mr Mack must straighten out the management team—quite possibly by bringing in past executives, like himself, and outsiders to serve alongside the current lot. He must also devise a strategy behind which his company can unite, selling what does not fit—preferably, before employees quit, as Morgan Stanley's people have lately been prone to doing. He faces a formidable task, notwithstanding the accolades that have been tossed in the returning hero's direction.

Typically, chief executives are given a few months' grace. Mr Mack's appeal, though, is that the three decades he spent at Morgan Stanley, and his subsequent spell atop Credit Suisse First Boston (CSFB), another leading investment bank, should allow him to move quickly. As recent events at Morgan Stanley show, times can change fast. The first signs of serious trouble came only in April, as top bankers quit and disgruntled ex-executives grumbled about Philip Purcell, then chief executive. Mr Purcell quit in June. The search for his replacement was supposed to take months. It took days, and ended with the choice of a man once purged by Mr Purcell and whom the board had specifically ruled out of the running.

Mack's pack

Mr Mack's return will not be cheap. His five-year contract will bring him 500,000 restricted shares, worth $27m at current prices, and a total annual package worth at least the average paid to the chief executives of the other leading banks, or $25m. The contract allows Mr Mack's retirement benefits to be calculated as if he had never left. The total cost of the change should become clear when the bank discloses how much it cost to show Mr Purcell the door.

Since replacing Mr Purcell on June 30th, Mr Mack has made a triumphant tour of his domain, including the trading floor and the headquarters of the retail brokerage. Merely showing his face has put him on a different plane from his predecessor, who was reclusive and uninspiring. Mr Mack can be charming and clever, and is willing to trawl for clients: all this is much appreciated in a firm short of morale. Many Morgan Stanleyites no doubt feel that Mr Mack was worth almost any price.

And yet, despite Mr Mack's virtues and the piles of recent laudatory articles, it is not altogether apparent that he is the man for the job. As Mr Mack acknowledges, his two biggest challenges will be devising a cohesive strategy and attracting top-notch employees. His record is not great in either area. He was president of Morgan Stanley in 1997 when the firm merged with Mr Purcell's Dean Witter Discover: the combination both cost him his job and created the problems he has been brought back to solve. The first time around, many at Morgan Stanley were glad to see him go.

Between 2001 and 2004, Mr Mack led CSFB, where the required skill was not to attract staff but to sack them. (However, his predictable nickname, “Mack the Knife”, dates from his first spell at Morgan Stanley.) Although a lot of money was saved, CSFB's ranking in the league tables broadly declined. This may have been especially costly in fixed-income underwriting, given the strength of bond markets at the time. In the end, his strategic answer to CSFB's troubles was to sell the firm. This may have been right, but it was an odd sort of salvation. The bank's Swiss board disliked the idea, and Mr Mack left.

That said, a decent defence of Mr Mack's record can be made. When he arrived at CSFB, says Guy Moszkowski, an analyst at Merrill Lynch, the firm was listing under an ill-timed, ill-priced, ill-advised merger; its franchise in technology underwriting had crumbled beneath a market crash; and its most prominent investment banker, Frank Quattrone, was facing charges that would eventually place him behind bars. Given all this, holding the firm together was an achievement. As for the Dean Witter deal, the results may have been the fault of poor execution under Mr Purcell. Mr Mack now has a chance to show he can do better.

He is likely to begin by making changes in Morgan Stanley's retail-broking arm. This is the heart of the old Dean Witter business and it is doing badly. Mr Mack has already noted Citigroup's recent swap of its asset-management arm for Legg Mason's brokerage operation. In the current regulatory environment, with watchdogs seeing conflicts of interest everywhere, the two businesses may not be compatible.

Changes in the institutional side of the business will be even trickier. Mr Mack has said that he would welcome back many of the executives who left recently and that he would like to lure other high fliers. For the moment, there may be a pause in departures, as bankers who either despised Mr Purcell or were unsettled by the turmoil no longer have cause to leave; but if Morgan Stanley looks vulnerable, head-hunters will be waiting.

Since his return, Mr Mack has remarked that broad-based financial firms seem to do particularly well—meaning, presumably, firms with the balance-sheet strength needed for lending as well as the knowledge needed for underwriting. That might point to a merger with a big bank. No one would be surprised if two years from now, when the guaranteed portion of his contract expires, the firm is transformed. The question is, will it be better off?

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Reforming the OECD

Changing of the guard

Jul 7th 2005
From The Economist print edition

An economic club and its governance

OVER the next few weeks, the race to become the next secretary-general of the Organisation for Economic Co-operation and Development (OECD) will quicken. The deadline for nominations for the successor of Donald Johnston, who steps down next year, is July 15th. In the background, however, there is a heated squabble over how to reform the Paris-based organisation's internal governance.

The OECD is essentially the economic-policy research unit of 30 rich (or aspiring) nations, establishing guidelines on everything from telecoms liberalisation and farm subsidies to macroeconomic policy. The oversight of the OECD is undertaken by a huge diplomatic staff from member countries. It entails more than 100 formal meetings annually. Because the turnover of national delegates is quick, their contribution is often not great.

Before discussions move ahead about enlarging the group—to those new members of the European Union not already in the club and to emerging economic powers such as China, India, Russia and Brazil—the OECD is trying to push through important internal reforms. Controversially, Mr Johnston has questioned the merits of those large diplomatic delegations, in a confidential report to finance ministers, seen by *The Economist*. Almost 400 national delegates are posted in Paris, costing as much as $130m annually, Mr Johnston wrote in a supplementary letter to ministers in May. (The OECD's working budget for its 2,000 staff is €3329m, or $392m.)

A shift to more control from capital cities should save money. Most OECD staff work directly with experts in national agencies rather than through the diplomatic intermediaries anyway. Yet the reform proposal is being stymied, because the diplomats have little incentive to consider recommendations that threaten to end their pleasant Parisian lifestyles. Even a suggestion that a group of “wise men” might provide an independent review of the OECD's internal practices was shot down by national delegates. Instead, the ambassadors agreed to establish a task force that includes themselves.

Some reforms are getting a hearing. America has proposed that the OECD's council meet only four times a year, instead of twice a month. It also wants new procedures for setting work priorities, voting rights and budget matters. No wonder, when it provides one-quarter of the OECD's main budget.

The challenges of reform and enlargement will face whoever takes over. Mr Johnston can press for reform because he has nothing to lose and wants to set the stage for his successor. Ironically, governments that normally welcome the OECD's advice on economic reform are resisting its recommendations for the group's own practices. The market power of incumbents is always difficult to shift.

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Carbon trading

Revving up

Jul 7th 2005
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Money is piling into Europe's new markets for pollution permits

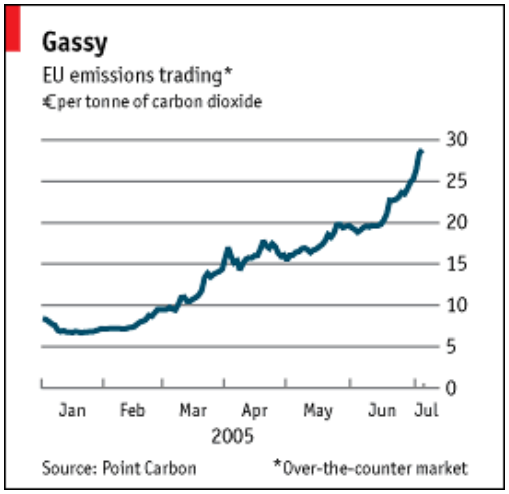
IF ONLY melting icebergs looked up with the eyes of hungry children, global warming might have stood a chance at Gleneagles. But Europe's new carbon markets aren't hanging around for substantive new measures from the G8. Prices, participants and volumes are increasing quickly.

The Kyoto treaty, which came into effect in February, saw an international emissions-trading system as one weapon against greenhouse gases. The idea is that a market-based system which gives countries and companies flexibility to meet their targets will produce the greatest emission reductions at the lowest cost.

Already Britain (in 2002) and then the European Union (from January 2005) have set up trial systems for carbon dioxide, the biggest of Kyoto's greenhouse gases. Europe's energy and industrial plants are being issued tradable annual allowances for emissions. Polluters that cannot squeeze under their caps buy the surplus of light polluters. The right wrists are slapped, and emissions overall are reduced at a lower cost than if each installation had had to meet an individual target.

Though the markets stuttered into life, they have grown surprisingly quickly. Volumes traded recently topped 2.2m tonnes a day. New exchanges are appearing: Austria launched an energy exchange on June 28th. Older ones are consolidating: Amsterdam's European Climate Exchange is joining Paris's Powernext to offer spot and futures contracts on the same screen.

What has made headlines, however, is the recent surge in the price of carbon allowances. On July 4th, it touched €29.35 ($34.90), a record (see chart). The cost of the allowances to produce one kilowatt-hour of coal-fired power is now greater than the cost of the coal itself, reckons Louis Redshaw of Barclays Capital.



Many reckon that the rise in emissions prices simply mirrors the rise in gas prices. When gas is dear, as it is now, utilities use more coal; because coal is dirtier, they have to buy more pollution permits in penance. And a heatwave in Europe since late June has dried up hydro power in the Iberian Peninsula and in Scandinavia.

Others, however, see a structural imbalance between supply and demand that may be harder to resolve. One reason why demand is outstripping supply is that a lot of firms that might have permits to sell are not yet participating, especially in new EU member states where allocation registries have not yet been set up. Many smaller firms do not have credit ratings and credit lines, so others are reluctant to do trades for future delivery with them, points out John Marlow of Rabobank.

The shortage, if there is one, may be eased by credits from projects outside Europe. Under Kyoto's Clean Development Mechanism (CDM), rich-country companies can earn certified emission reductions (CERs) by cleaning up emissions in developing countries. The EU allows them to be used to comply with caps. There is a rush to do just that, especially since CERs are changing hands for €7 or €8 and European allowances are heading for €30.

Europe's carbon-trading markets have a touch of the Wild West about them. At least two-thirds of the trades are over-the-counter and relatively opaque. Though part of the huge price gap between CERs and allowances is justified by the former's greater riskiness, it nonetheless invites swingeing arbitrage. “It's an emerging market with an awful lot to learn,” says James Cameron, chief executive of Climate Change Capital, a small investment bank, but he is confident that there is plenty of interest in just these sorts of strategies.

That people will make—and lose—money in the carbon markets seems assured. But will the markets help to reverse global warming? At these volumes, no. “It is just one tool but a very important tool,” says Elliot Morley, climate-change minister at Britain's agriculture department. Now, if only his boss could persuade George Bush to follow suit.

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Secured lending

Thinner

Jul 7th 2005
From The Economist print edition

Britain's highest court rules on the standing of certain secured loans

A LEGAL case concerning the precise status of a loan by a British bank to a now insolvent paint firm might sound as interesting as, well, watching the defunct debtor's products dry. However, financial institutions that have made secured loans to companies under English law—used in many transactions around the world—will have paid close attention to the final resolution of this test case late last month in Britain's highest court, the House of Lords.

At issue was whether National Westminster Bank had successfully taken fixed-charge security over the debts of Spectrum Plus, a paint company that went into liquidation in October 2001. A fixed charge puts a lender at the front of the queue of creditors should a borrower go bust. With a floating charge, however, a lender has to wait behind others, and thus faces a greater risk that it will not get its money back.

Until recently, banks had taken comfort from a 1979 High Court case known as *Siebe Gorman*. In essence, lenders considered that they had a fixed charge if they and their borrowers had so agreed. Last year, however, NatWest asked the High Court whether the security given to it by Spectrum Plus, which was identical to that in *Siebe Gorman*, did indeed amount to a fixed charge.

In summary, the High Court said that it did not. Three judges in the Court of Appeal reversed that decision, but gave permission for an appeal against their ruling to the House of Lords. Seven judges there agreed unanimously with the High Court. Spectrum Plus, they said, gave NatWest a floating charge over its debts and proceeds, not a fixed one. *Siebe Gorman* was wrong.

The Lords thus ended a debate which had surfaced in New Zealand in 2001. Senior English judges, hearing the final appeal, said that whether a charge was truly fixed or floating depended not on how the parties described it on paper, but on how much control the borrower had over the charged assets.

The British government will benefit from the Lords' ruling. Until the law changed in 2003, some government departments were next in the queue after fixed-charge holders when firms went bust. Hundreds of liquidations were halted pending the result of this case. Now that the Lords may have turned some supposedly fixed charges into floating ones in a number of these liquidations, the government should gain.

The ruling will apply retrospectively and may lead to similar challenges to fixed charges. It may also prove costly to some small companies, because it may provoke lenders to seek personal guarantees from these firms' directors, as well as fixed charges. But the Law Lords have at least clarified the law in this difficult and controversial area for bankers and bankrupt borrowers alike.

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Terrorism insurance

Predicting the unpredictable

Jul 7th 2005
From The Economist print edition

Preventing terrorism is wretchedly difficult. So is insuring against it

AP

Dogged defender

THE explosions in London on July 7th were an awful reminder of how difficult it is to predict such events. Yet specialists in the insurance market try to do just that, using computers to simulate the effects of explosions so that insurance can be priced. They are experts in terrorism insurance, striving to make their models quantify the threat to commercial interests.

The market has already seen, among other things, political terrorism in Colombia and the bomb blast in Bali in 2002. Ascot, a syndicate at Lloyd's of London, paid a claim earlier this year on a Beirut property damaged in the explosion that killed Rafik Hariri, a Lebanese politician. Most risk experts balk, though, at the mention of attacks with chemical, biological, radiological and nuclear (CBRN) weapons. “We don't feel we've got a cheque big enough to pay for that eventuality,” says Stephen Ashwell of Hiscox, another Lloyd's syndicate that writes terrorism-risk policies.

Two new reports published in the week or so before the London blasts—one from America's Treasury, the other from the OECD—look at terrorism risk and commercial strategies for coping with it. The former puts great faith in private insurers' ability to meet the costs of future terrorist attacks in America. The latter, which takes a global view, is much less optimistic.

To the chagrin of America's property insurers, the Treasury argued against the extension, in its present form, of a government reinsurance scheme to back them up in the event of another big terrorist attack. The scheme, known as TRIA, was created in 2002 as a short-term means of stabilising the private sector, which faced claims in excess of $30 billion from the attacks of September 2001. The Treasury says TRIA has met its goal. Its fate will be decided in Congress later this year; if it is extended, the Treasury says, private insurers should be expected to absorb more risk.

That may mean higher premiums, or less cover, for policyholders. Many property insurers are now writing “sunset clauses” into new policies that will leave some clients with potential gaps in terrorism-risk coverage should TRIA expire at the end of the year. Terrorism-risk premiums are likely to rise in Manhattan, as well as downtown Chicago, San Francisco and Los Angeles. The handful of insurers providing separate terrorism-risk coverage—a clutch of Lloyd's syndicates, a few firms in Bermuda, American International Group, ACE and Berkshire Hathaway's National Indemnity—are cautious about adding exposure in these cities, because of high building density and the extensive coverage they have already written. This may worry property developers, because many lenders now require terrorism cover as a condition for financing big projects.

The OECD report, published on July 5th, offers a rather different view. It says that private insurance is best, but that there is a role for government in countries where private capacity is insufficient. Government schemes of some sort exist not only in America, but also in Australia, Britain, France, Germany and Spain. The OECD worries specifically about CBRN threats, which are generally excluded from private policies and are not covered by some government programmes.

The number of companies insured against terrorism varies greatly by country. In France, Spain and Australia, coverage is obligatory; in Britain, it is optional, but a history of terrorist attacks and an affordable government scheme called Pool Re mean that many firms are covered. But the OECD voices concern about take-up rates in Germany, where a mere 3% of companies are covered. It also worries about America, where it thinks that “the economic and social impact of a new large-scale attack could be

greater than in 2001." In America, about half of companies had such insurance in 2004. Insurance brokers say firms in financial services, property and health care led the way: 60% or more were covered last year. But manufacturers, drugmakers, chemicals firms and energy companies lagged far behind, and some of these face obvious terrorist threats.

Underwriters like to suggest they have the problem under control. But the very nature of terrorism—great uncertainty about when and where an attack comes, and how bad it might be—makes this a peculiarly subjective area of insurance underwriting. Like terrorism itself, for the insurance industry this is not a problem that is likely to disappear soon.

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Economics focus

Displacement activity

Jul 7th 2005
From The Economist print edition

Do immigrants take our jobs? Only if we try too hard to preserve them

ON APRIL 20th 1980, Fidel Castro, Cuba's president, declared Mariel harbour an “open port”, inviting those Cubans who wished to leave his country to do so. Many accepted eagerly. Between May and September, about 125,000 of them were ferried to America by a flotilla of fishing vessels, yachts and shrimp boats, often chartered by Cuban exiles in Florida.

In 1992, Bosnia-Herzegovina declared its independence from Yugoslavia. A month later, the Bosnian Serbs laid siege to Sarajevo, Bosnia's capital. That year, almost 234,000 Yugoslavs applied for asylum in safer European countries.

The Mariel boatlift, as it was called, and the Balkan wars have provided two of the more interesting “natural experiments” in the economics of immigration. Both have allowed economists to cut the Gordian knot entangling immigration's impact on the economy and the economy's impact on immigration. Often, cities and countries that host the most immigrants also boast the best economic performance. That might be because immigrants bring prosperity; but it might be that they are attracted by it. Awkwardly, to the commonest question—do immigrants take our jobs?—the two experiments offer different answers.

The Marielitos who settled in Miami added about 45,000 workers to the city's labour force, an increase of 7%. In a seminal study published in 1990, David Card, now of the University of California, Berkeley, concluded that the city's economy took the new arrivals in its stride. The murder rate rose that year, he reported, and riots broke out in the summer. But Mr Card found no indication that the Marielitos cost the city's non-Cuban residents their jobs or depressed their wages.

His sanguine conclusion is not widely shared on the other side of the Atlantic. Europeans still incline to the view that immigrants usurp the jobs held by natives, according to a survey* of public attitudes by Christian Dustmann and Albrecht Glitz of the Centre for Economic Policy Research. These worries may be well founded. A 2003 paper† by Joshua Angrist, of the Massachusetts Institute of Technology, and Adriana Kugler, now at the University of Houston, uses the break-up of Yugoslavia to shed light on how Europe's labour markets respond to foreign arrivals. They show that a country's distances from Sarajevo and Pristina were good predictors of immigration during the Bosnian war and the Kosovan war (in 1999) respectively. Thus if native workers fared worst in the countries closest to these cities, this is evidence that immigration can hurt their fortunes. The authors estimate that in a country similar to Germany, 100 new arrivals from outside the EU could displace between 35 and 83 native men from their jobs.

Miami virtue

Why did Miami cope so well with its sudden influx of new workers, while Europe struggled so badly? In a paper†† last year, Ethan Lewis, of the Federal Reserve Bank of Philadelphia, looked at Miami's mix of industries before and after the boatlift. Perhaps some industries expanded to accommodate the kind of unskilled labour most of the Cuban boat-people could offer? The garment industry, for example, was used to hiring Cubans and might have taken up any slack. But Mr Lewis finds little evidence of such a shift. Miami's manufacturing complexion broadly resembled that of other cities in the south and mid-west in the 1980s, just as it had in the 1970s.

Mr Lewis offers a different, surprising explanation. As a result of the boatlift, Miami's firms were slower than rivals elsewhere to adopt technologies, such as computers, that have taken over some of the routine, codifiable tasks performed by unskilled workers. With so many willing, untrained workers

available, the city's joiners, bakers and electrical-equipment makers felt under no great pressure to replace men with machines. By 1984, for example, 36% of people in Houston used computers at work. But in Miami only 23% did. The impact of the boat-people was visible not in the things Miami made, but in how it made them.

Many politicians now argue that they should pick the type of immigrants their economy “needs”. But as Mr Lewis shows, what an economy needs is not written in stone. Flexible economies take advantage of whatever labour lands on their shores.

Why did Europe's economies fail to adapt? Mr Angrist and Ms Kugler suspect that government efforts to preserve jobs backfired. In many parts of Europe, for example, governments try to protect workers by making it more costly to fire them. But workers that are expensive to fire are also dear to hire. Immigrants—often recruited on temporary visas, beyond the embrace of unions and sometimes outside the law altogether—become more attractive by comparison. Because they cannot become ensconced in a job, they are more likely to be offered one. In the short run, this kind of immigrant competition undercuts wages and raises profits. In the long run, however, higher profits should tempt new firms to enter the market, compete for workers and bid wages back up.

In Europe, sadly, the long run never arrives. The entry of new firms is inhibited by regulations to protect old ones. Mr Angrist and Ms Kugler show that the higher the barriers to entry in a country are, the worse is the impact of immigration on the job prospects of its citizens. Intended to shield small players from competition, these regulations instead provide for stagnation. Perhaps Europe's politicians should worry less about repelling immigrants, and more about unshackling the firms that might employ them.

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* “Immigration, Jobs and Wages: Theory, Evidence and Opinion”: May 2005.

† “Protective or Counter-Productive? Labour Market Institutions and the Effect of Immigration on EU Natives”. *Economic Journal*, June 2003.

†† “How Did the Miami Labour Market Absorb the Mariel Immigrants?”: www.phil.frb.org/files/wps/2004/wp04-3.pdf

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Correction: sugar subsidies

Jul 7th 2005
From The Economist print edition

A recent story on sugar subsidies ("Beet a retreat", June 25th) wrongly attributed a study of the sugar market to David Pearce of University College, London. The study was actually co-written by David Pearce of the Centre for International Economics, Canberra. Our apologies to them both.

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Nuclear weapons

Under new management

Jul 7th 2005
From The Economist print edition

KOBAL

America's atomic-bomb laboratories are about to be overhauled. It promises to be a tricky business

Get article background

JUST over 60 years ago, Robert Oppenheimer demonstrated the power of a partnership between the American government and academia. His team of university scientists developed and built the first nuclear bombs in a jumble of buildings at Los Alamos in the New Mexican desert. The team achieved its astonishing success in just over two years.

The University of California has run Los Alamos National Laboratory since that inception in 1943. But an embarrassing series of security and safety lapses at the laboratory, which recently resulted in the temporary suspension of all classified work for several months, has led the government to insist that the university find an industrial partner when it rebids for the contract to manage the place on July 19th. The contract is open to competition, and a rival bid is expected from another university with a commercial partner.

Los Alamos is one of three national laboratories working on nuclear weapons. For more than half a century, the University of California has run two of them—Los Alamos and Lawrence Livermore National Laboratories, which specialise in nuclear science—on behalf of the American government. The third—Sandia National Laboratories, which is responsible for the non-nuclear components and systems engineering for America's nuclear weapons—is managed by Lockheed Martin, an engineering firm. The contracts for managing all three will now be put out to tender.

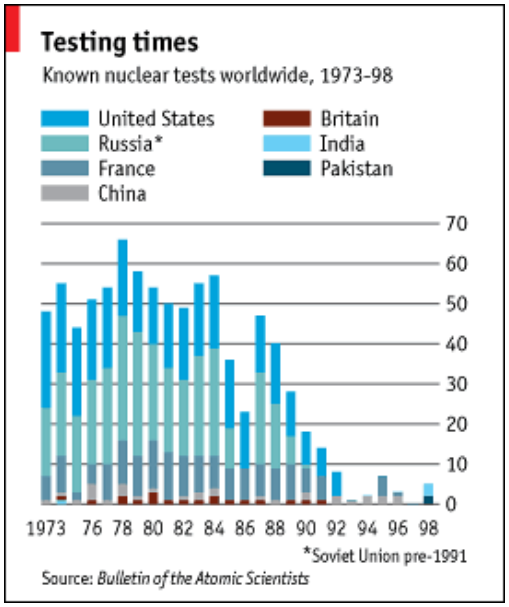
Work at the labs has shifted considerably since the testing of nuclear weapons was suspended in 1992. Instead of weapons development, America's nuclear-weapons scientists have been engaged in “stockpile stewardship”, a programme designed to ensure that the country's warheads will continue to function predictably as they age. This work involves computer simulations of how a weapon would explode, and “subcritical” tests that do not involve full nuclear detonations.

The labs have two large physics experiments under way. The first, at Los Alamos, is an oversized X-ray machine that uses non-fissile material to examine what happens when a pit—the fissile core of a nuclear weapon—implodes. In a weapon, this implosion triggers the nuclear explosion; in the lab, the explosion is thankfully absent. The second experiment is the National Ignition Facility (NIF), which is intended to

generate temperatures and pressures approaching those created by the pits, in order to detonate small pellets of nuclear explosive.

Politics is currently threatening the NIF, which is being built at Lawrence Livermore, in California. It was supposed to be completed, at a cost of $1.4 billion, in 2003. To date, $2.8 billion has been spent on it—a figure somewhat complicated by the mingling of construction and running costs—and the facility is still an estimated four years from completion.

On July 1st, the Senate voted to stop construction completely, action that was part of a $31 billion energy and water appropriations bill. Pete Domenici, a Republican Senator from New Mexico who heads the relevant subcommittee, made the proposal. His state includes both Los Alamos and Sandia (though Sandia also has a site in California).



Although the decision appears to threaten the facility, it could be just a piece of political manoeuvring. John Pike, director of GlobalSecurity.org, a Washington-based defence consultancy, wonders whether Mr Domenici might be positioning himself for a meeting later this summer, when he must get together with members of the appropriations committee of the House of Representatives, whose chairman is from California and therefore unlikely to agree to the cuts. Nevertheless, Mr Pike says, there are still questions to be asked about the role of the ignition facility.

Most researchers agree that the NIF is scientifically important for the study of nuclear fusion; more controversial is whether it is necessary for stockpile stewardship. Sidney Drell, a physicist and arms-control specialist at the Stanford Linear Accelerator Centre, in California, says the project is “integral” to stockpile stewardship. Mr Pike, however, describes it as a “self licking ice-cream cone—a thing that exists for its own sake and serves no purpose”. Some physicists agree, though not on the record.

Three recent internal reviews of the facility by the Department of Defence and the Department of Energy go so far as to suggest that without it America would move closer to resuming nuclear testing. The longer the country relies solely on computer simulations to check for faults, rather than on the micro-explosions the NIF would make possible, the less certain the Department of Defence is that the warheads will perform as expected.

But stockpile stewardship has other functions. It retains a coherent body of nuclear expertise in America and (which is slightly different) it prevents nuclear scientists from being lured overseas. Unfortunately, the uncertainty about the future has lowered staff morale, potentially damaging this secondary function of keeping weapons scientists in America. At Los Alamos, the appointment of an irascible former admiral as the lab's director did not help, although he has since been replaced. An unofficial blog that allows disgruntled staff to publish anonymously lists gripe after gripe. Older staff—some 39% are aged 50 and above—have been retiring at unprecedented rates, afraid that their generous pension packages will be cut if the University of California fails to win the contract. At Lawrence Livermore, some 300 researchers were made redundant last year after Congress slashed the NIF's construction budget.

Yet there is hope for a brighter future. A fundamental rethink of the way in which America maintains its nuclear weapons is on the cards. Congress recently authorised a two-year study to determine whether a new approach to maintaining warheads would be possible. The so-called reliable replacement warhead programme aims to work out whether it is possible to make cheaper weapons without nuclear testing, by modifying existing components. The programme could present opportunities for demoralised nuclear scientists.

Historically, the University of California has managed the labs on a not-for-profit basis. To encourage competition for the management contract, officials at the Department of Energy plan to increase the management fee, to allow an element of profit. Indeed, a University of California internal memo reads, “Extrapolating from a recently negotiated DOE contract with Lockheed Martin to manage Sandia, we imagine we could double the $15m fee.” Higher fees should secure better management and improved working conditions for staff.

After much soul searching as to whether the university should be conducting nuclear work at all, its senior management has decided to go ahead with a bid in partnership with Bechtel, an engineering and construction firm based in San Francisco. The University of Texas has announced it will also bid for the contract, in partnership with Lockheed Martin.

Whichever succeeds—the result will be announced by December 1st—it is probably a smart idea to keep the nuclear-science labs managed at least in part by academics. Historically, university management has proved better for long-term research projects than corporate governance. The research culture at universities is open and flexible. This attracts talented scientists and stops them wandering to places where their talents might be put to uses of which the American government might disapprove.

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Space exploration

Dispatches from the void

Jul 7th 2005
From The Economist print edition

NASA probes beam a wealth of data to Earth

IT HAS been an up-and-down year for America's space agency, NASA. While the space shuttle has been dogged by delays and safety concerns (if all goes well, “return to flight”, as the NASA spin machine dubs the next shuttle mission, should happen on July 13th), the agency's unmanned missions have been unmitigated successes.

Reuters

A Tempel of science

On July 4th NASA's cometary probe *Deep Impact* lived up to its name by knocking a hole in comet Tempel 1 (pictured right) and creating a plume of gas and dust that researchers back on Earth are now analysing. Meanwhile, half a dozen papers have been published in *Nature*, summarising the findings of *Spirit* and *Opportunity*, two robot rovers that have been trundling over the surface of Mars since January 2004, which is 15 months longer than planned.

The question everybody wants to answer, of course, is “is there life on Mars?” The rovers were not designed to address that question directly. But they were definitely intended to ask whether there had ever been enough water lying around for life as known on Earth to have emerged. Indeed, *Spirit*'s landing site, Gusev crater, was chosen because it looked as though the crater might once have contained a lake.

Unfortunately, that turned out not to be the case. Spectroscopic analysis of Gusev's rocks suggested that, rather than originating in an ancient lakebed, they were of volcanic origin. That does not mean there was never any water at all in the crater, though. One of the research groups writing in *Nature* concluded that highly acidic water had once been present in Gusev, probably in the form of thin films, and that it interacted with the volcanic rocks there, leaving behind tell-tale minerals. But it is unlikely that there was ever enough of this water to form pools—in contrast to previous reports from *Opportunity*'s landing site, where the presence of haematite, an iron-oxide mineral that often forms in the presence of water, suggests there had, indeed, once been pools.

How widespread those pools were, though, is a moot point. The presence in Martian dust of a mineral called olivine, which disintegrates rapidly in the presence of water, suggests that even if liquid water was ever widespread, it was not around when the rocks from which the dust formed were created.

All of which goes to show that although the rovers have worked better than could reasonably have been hoped for, studying a couple of random spots on the surface of a planet is likely to raise as many questions as it answers. Which, if America's taxpayers remain willing, is good news for Martian scientists, who will thus remain employed for years to come.

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Human behaviour

The smell of power

Jul 7th 2005
From The Economist print edition

Odour and mating preferences

WHAT'S a girl to do when faced with the choice between a powerful action man who has great DNA but is likely to love her and leave her, and a carpet-and-slippers kind of bloke who will hang around and bring up the kids but may not be Mr Right in the genes department? Well, ideally, she should fool the latter into bringing up the former's children. And a piece of evidence that this is exactly what happens emerged this week from a research group led by Jan Havlicek of Charles University, in Prague.

Dr Havlicek and his colleagues were interested in discovering whether women are attracted by the smell of dominant men. A preference for the scent of dominants has been found in the females of other species, and scent is known to be important in attraction between the human sexes in other contexts, such as avoiding inbreeding. The attractiveness of body odour is also correlated with the attractiveness of the body it came from, even when presented separately from that body. But whether the odour of power—or, at least, of powerfulness—is attractive to women had not been established.

Deciding who is and is not a dominant male is the first question, of course. To do this, the researchers turned to one of the world's most widely used experimental animals, the hard-up male student. Their subjects were asked to rate such things as their tendency to correct others, to want to control conversations, and to surpass others' accomplishments, in a questionnaire designed to assess their dominance. In their paper in *Biology Letters* the researchers laconically observe that dominance in this questionnaire “corresponds to the scale ‘Narcissism’ in the widely used California psychological inventory”.

After baring their all in this manner, the volunteers had to wear cotton pads under their armpits for 24 hours to collect the sweat therefrom, and also had to lay off curries, beer, cigarettes and similar delights of student life that might affect the smell of their sweat. Surprisingly, given these constraints, the researchers managed to persuade 48 men to volunteer.

Compared with this, the female volunteers had it easy. They had to smell the pads and rate them for “intensity”, “sexiness” and “masculinity”. Okay, perhaps not that easy. They also had to vouchsafe whether they were single or in an on-going relationship with a man, and to submit to a saliva test that would show the phase of their menstrual cycle.

The upshot of the trial was that women did, indeed, find the odour of dominants sexier than that of wimps—but only in special circumstances. These circumstances were first that the woman was already in a relationship and second that she was in the most fertile phase of her cycle. In other words, dominant males' scent was only more attractive at the point where a woman could both conceive and cuckold her mate. Which, given previous studies that show dominant men are indeed more likely than others to leave a woman holding the baby, makes perfect sense.

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Anthropology

Taiwan, twinned with Hawaii

Jul 7th 2005
From The Economist print edition

Polynesians are Taiwanese in disguise

MAORI legend has it that Polynesians originated from a place called “Hawaiki”. Where Hawaiki was located is a mystery. But the toings and froings of the Polynesians—arguably the greatest seafarers in history—have long intrigued researchers of an anthropological turn of mind, and two of them, Jean Trejaut and Marie Lin of Mackay Memorial Hospital in Taipei, think they know the answer to the riddle of Hawaiki: Taiwan.

This is not a total surprise. Linguistic evidence pointed that way already. But, in a study just published in *Public Library of Science Biology*, Dr Trejaut and Dr Lin nail the question down with that talisman of modern research, genetics.

Present day Taiwan has a population of 23m, but only 400,000 are descended from the island's original inhabitants (the majority of the population is descended from mainland Chinese who have settled there over the past 400 years). Those 400,000 speak—or, at least historically spoke—languages belonging to a group known as Austronesian, which is unrelated to Chinese, but includes the Polynesian tongues. Indeed, small though the aboriginal Taiwanese population is, it accounts for nine of the ten linguistic sub-families of Austronesian. Hence the supposition that Hawaiki might be Taiwan.

To check this out, Dr Trejaut and Dr Lin decided to look at variations in mitochondrial DNA. This is passed from mother to offspring without genetic admixture from the father, because it is found in the bodies of cells—including, crucially, egg cells—rather than in the cell nuclei where the rest of the genes reside. (Sperm jettison their mitochondrial DNA at fertilisation.) That makes tracing mutations through the generations easier than looking at those genes that get mixed up by sex.

In a study involving 640 people from nine Taiwanese tribes, Dr Trejaut and Dr Lin found three mutations shared by Taiwanese, Polynesians and Melanesians (who also speak Austronesian) which are not found in other Asians. So the mystery seems to have been solved at last. Where the Taiwanese came from, though, is a different question again.

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The Eternal City

So close, and yet so far

Jul 7th 2005
From The Economist print edition

Reuters

Rome has always managed to embody both heaven and hell

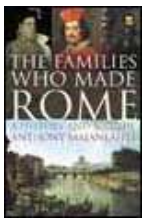
WITH its heady mix of earthy effluence and celestial protectionism, Rome simply cannot leave you cold. Some visitors, such as Dante, Montaigne, Byron, Zola and Garibaldi, were overwhelmed by the atmosphere of indolence and torpor, the malign, fetid air of the Tiber and the Pontine Marshes, and the *mal'aria*, which every summer brought in its wake an epidemic of deadly fever. Others saw only the city's luminosity: Campo dei Fiori in the lemony light of early morning, the pinky breast of St Peter's dome, the enchanted sky that Alfred de Musset, a 19th-century French romantic, described as “so pure that a sigh rises to God more freely than in any other place on earth.”

The spiritual significance of Rome, home to the successors of St Peter, the rock on whom the Christian church was built, plays a central part in the magic of the Eternal City. That spirituality has a bulwark in physical symbols too. At their best, these creations are an important reminder of the effort that humankind has made over the ages to strive for the sublime—and a warning, for those who care to think, of how all too often it is brought low by failure.

Rome shrank, during the Black Death and the removal of the papacy to Avignon in the 14th century, into two parts: the *disoccupato*, an outer ring of broken arches, empty houses and abandoned fields, and the *occupato*, a small kernel of settlements that clung to the banks of the Tiber hoping for better times. Two centuries later, spiritual and temporal stepped once more in tandem with the start of the Counter-Reformation and the papal restoration.

This shift, which was felt immediately in an increase in economic activity—more visitors, more traffic, trade and construction—would lead to a significant expansion of the *occupato*. It also coincided with the beginning of the Renaissance and a growth in the number of artists flocking to the city. In “The Families Who Made Rome”, Anthony Majanlahti, a Canadian historian and fellow of the British School at Rome, maps the network of patronage that supported the artists whose work would transform the city skyline: the Colonna, who built one

The Families Who Made Rome: A History and a Guide
By Anthony Majanlahti



Chatto & Windus; 418 pages; £20

Buy it at
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The Genius in the Design: Bernini, Borromini and the Rivalry that Transformed Rome
By Jake Morrissey

of Rome's most grandiose Baroque gallerias, the della Rovere (the first of the Roman families whose nephews, or *nipoti*, would enjoy such papal favour they gave birth to the word "nepotism"), the Farnese whose sumptuous palace now houses the French embassy, Gianlorenzo Bernini's patrons the Borghese, Francesco Borromini's early supporters the Pamphili, and the Chigi and the Barberini, whose grand palace in an 18th-century engraving by Giuseppe Vasi, seems magically to dominate and withdraw from the piazza in front of it.

In "The Genius in the Design", which came out in America in March, Jake Morrissey looks in detail at the work of two of the greatest of these Renaissance artists, and how the rivalry between them helped to transform Rome. Both sculptors and papal architects, Bernini and Borromini could not have been more different as men. Where Bernini was "subtle, gracious, diplomatic [moving] easily through the courts of popes and princes", Borromini was "difficult, argumentative, inflexible and quick to take offence". Born within months of each other, Bernini lived—and flourished—through ten pontificates and died in his own home in 1680 at the age of 81. In 1667 Borromini fell on his sword, literally, after a decade of disappointments, having quarrelled with all his patrons.

Despite their differences, or perhaps because of them, the two men were inspired and spurred on by their rivalry. They watched one another while they created their individual masterpieces: Bernini, the church of Sant'Andrea al Quirinale, and 300 yards away, Borromini's San Carlo alle Quattro Fontane. They collaborated over the task of finishing and decorating the papal basilica of St Peter's, and for a while were even in business together.

Despite a final falling out, they are jointly remembered: "If anyone invented the Rome we know today, it is Bernini and Borromini," Mr Morrissey writes. "It was their passion, their vision, which gave us the Rome of extravagant churches of travertine and broad piazzas of granite. The Rome of towering domes that reach toward God and expansive *palazzi* that declare the power of man."

William Morrow; 336 pages; $24.95
Duckworth; £20

Buy it at
Amazon.com
Amazon.co.uk

Rome or Death: The Obsessions of General Garibaldi
By Daniel Pick

Jonathan Cape; 288 pages; £16.99

Buy it at
Amazon.com
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Two centuries later, Garibaldi, the architect of the Italian Risorgimento, was dismayed when the city of the popes was left out of the newly unified Italian state. "Rome or Death" became his rallying call in the 1860s as he tried, vainly and repeatedly, to secure what he regarded as the nation's natural capital. In 1871, the Franco-Prussian war put paid to the regime of Emperor Louis Napoleon, thus ending France's support for the papacy which allowed Rome to be absorbed within the Italian fold.

Less than four years later, Garibaldi left his island retreat in the Mediterranean and took up a new cause to subjugate the landscape of the Eternal City: diverting the graveolent, disease-ridden River Tiber away from Rome by building over it a Parisian-style boulevard, which he dreamt would become a wonder of the modern world.

In a fascinating dissection of a slice of European history, Daniel Pick, a psychoanalyst and professor of history at the University of London, examines Garibaldi's deeper motives in wanting to purify the papal city. He looks at how he was affected, in part subconsciously, by his inability to save the life of his beloved first wife, Anita, after they fled Rome amid revolutionary turmoil in 1849, his later failure to secure the holy city as the capital of the newly born nation and his anger at the papal establishment which he felt had betrayed the city during a terrible flood in which the Tiber broke its banks on Christmas Day 1870.

Garibaldi's Roman scheme fell foul of political indolence and financial constraints. But his obsession for the holy city—like that of Bernini and Borromini before him—helped make Rome unique.

The Families Who Made Rome: A History and a Guide.
By Anthony Majanlahti.
Chatto & Windus; 418 pages; £20

The Genius in the Design: Bernini, Borromini and the Rivalry that Transformed Rome.
By Jake Morrissey.
William Morrow; 336 pages; $24.95
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Rome or Death: The Obsessions of General Garibaldi.

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Srebrenica

Ten years on

Jul 7th 2005
From The Economist print edition

Tales of crime and shame

MILLIONS of words have been written about Srebrenica in the past ten years, many of them this week, the tenth anniversary of its fall. In a few days in July 1995, Bosnian Serb forces under General Ratko Mladic killed some 8,000 Bosnian Muslim men and boys. Most of the descriptions of this carnage may eventually be forgotten, but “Postcards from the Grave” should stand the test of time. It is the first book in English written about Srebrenica by a Bosnian who lived through its three-year siege—and survived.

The story begins in 1992 when, as a 17-year-old schoolboy, Emir Suljagic was forced to flee Serb paramilitaries and ethnic cleansers into the eastern Bosnian town of Srebrenica. He taught himself English and secured a job with the United Nations as a translator. It was this which was to save his life. Now a journalist in Sarajevo, Mr Suljagic provides a moving insight into the life, times and thoughts of his hometown, both in tragedy and comedy.

Side by side with the ripped flesh of the dead sometimes left hanging from the trees and wire fences to which they had been dispatched by exploding shells is the story of a family who blossomed after living off bread made with relief-aid milk powder. Alongside tales of mind-numbing fear comes also the grotesque: a local UN employee who survived what was called the “march of death”, trekking for 38 days across Serb-held territory to safety, only to be informed on arrival that he could not now go on holiday since he had just used up his annual entitlement.

Mr Suljagic is angry at the world which neither prevented the Serbs from seizing this UN-declared “safe area” nor saved the lives of his family, friends and people. He has every right to be. And yet he has written a beautifully turned work. He does not rant or insult; he just tells the story of Srebrenica. Nor does he balk at broaching difficult issues. Did Srebrenica's Muslim forces also commit war crimes against Serbs? Was their military leader a mafia boss as well as a great soldier? Mr Suljagic does not go as far as providing concrete answers to these questions, but the wonder is that he mentions them at all.

The tenth anniversary has proved a good excuse for publishers, Saqi Books leading them in a joint-venture with the Bosnian Institute, to bring out several more books on Bosnia and the war. “Raw Memory”, by two French journalists, reminds us, in a timely fashion, that Srebrenica, rather like Auschwitz, was not the only crime. This excellent book focuses on the ethnic cleansing of Bosniaks—as Bosnian Muslims are now called—in the northern town of Prijedor in 1992. Taking the story forward, it also shows how the UN's Yugoslav war-crimes tribunal, by removing key ethnic cleansers, has opened the way for a return home for many Bosniaks.

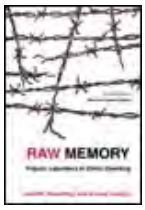
What gives the book its strength is its tale of extraordinary characters. One such is Muharem Murselovic, a Bosniak who survived the Bosnian Serb camp of Omarska. Now he passes it as he drives to take up his seat in the Bosnian Serb parliament.

Postcards from the Grave
By Emir Suljagic. Translated by Lejla Haveric

Saqi Books/Bosnian Institute; 240 pages; £12.99 and $24.95. To be published in America by Saqi Books in September

Buy it at
Amazon.com
Amazon.co.uk

Raw Memory: Prijedor, Laboratory of Ethnic Cleansing
By Isabelle Wesselingh and Arnaud Vaulerin. Translated by John Howe



Saqi Books; 292 pages; £14.99. To be published in America by Saqi books in August

Buy it at
Amazon.co.uk

Bosnians

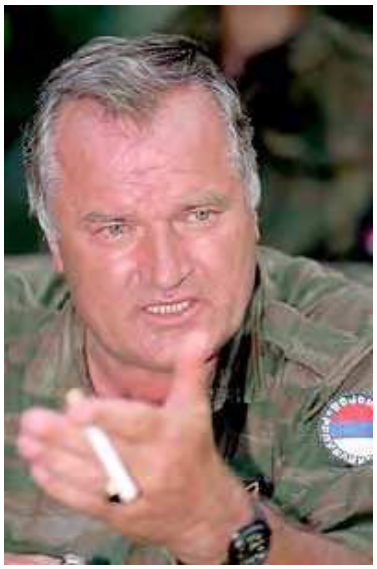
Paul Lowe's “Bosnians” is a collection of fine photographs taken both during the war and afterwards, some in Srebrenica. Here, there are moments of terror and tragedy, but love and laughter too. It is a shame, perhaps, that all of Mr Lowe's Bosnians, except for one or two pictures, come from the Bosniak side. But then, as Allan Little, a BBC journalist, says in a short but moving essay in the book, “Why did we become so enfolded...by a war that was not ours.” When it ended, he admits to an awful inner doubt: “Did I miss my war? Was I—the thought horrified me—somehow sorry it was over?”

While the theme of the other books is survival and triumph over adversity, “Sarajevo Rose”, by Stephen Schwartz, an American poet and writer, is drawn mostly from tales of Bosnia's fourth group of people after its Bosniaks, Serbs and Croats; its Jews who have now virtually vanished from the country. Mr Schwartz's book contains extraordinary and fascinating stories of Bosnia's Jews, many of whom came there after being expelled from Christian Spain in 1492.

Occasionally, his writing rambles or turns to a rant about Bosnia's war-time fate, and his academic inquiry may prove too dense for some lay readers. But Mr Schwartz has written a book that nobody else has, a fine achievement in an ever more crowded market.

Postcards from the Grave.
By Emir Suljagic. Translated by Lejla Haveric.
Saqi Books/Bosnian Institute; 240 pages; £12.99 and $24.95. To be published in America by Saqi Books in September

AFP



Mladic: why do monsters look so ordinary?

By Paul Lowe

Saqi Books; 172 pages; £18.99 and $35

Buy it at
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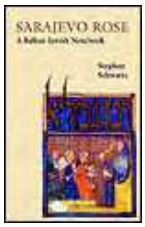
Amazon.co.uk

Sarajevo Rose: A Balkan Jewish Notebook
By Stephen Schwartz



Saqi Books; 288 pages; £16.99. To be published in America by Saqi Books in August

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Raw Memory: Prijedor, Laboratory of Ethnic Cleansing.
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Deep Throat

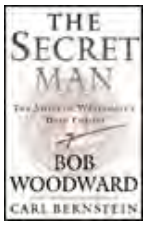
A principle to protect

Jul 7th 2005
From The Economist print edition

IT WAS one of the great mysteries of recent American history: the identity of Deep Throat, Bob Woodward's most secret and influential source for the Watergate stories that in 1972-75 made his and Carl Bernstein's reputation, brought down Richard Nixon and turned Ben Bradlee's *Washington Post* into a role model for a generation of journalists. Yet the answer, when it came in a *Vanity Fair* article on May 31st, was disappointingly mundane. Even so, Mr Woodward's new account of his relationship with Mark Felt makes compelling reading.

This most mysterious of men was simply someone whom Mr Woodward met by accident in a White House waiting room, when he was still in the navy and Mr Felt was a rising star in the FBI, and who became a source for Mr Woodward during his early days in journalism. By the time the Watergate burglary took place, in June 1972, Mr Felt was number two in the FBI. He resented having been passed over, as he saw it, for the succession to his hero, J. Edgar Hoover, and became angry when the White House started to block the investigation into Watergate. As Mr Woodward says, if you did not know Deep Throat's identity, it was not obvious; but if you did, it was entirely obvious.

The Secret Man: The Story of Watergate's Deep Throat
By Bob Woodward



Simon & Schuster; 256 pages; $23

Buy it at
Amazon.com
Amazon.co.uk

"The Secret Man" was rushed into print once Mr Felt's family disclosed his identity, but had long been on Mr Woodward's desk in draft form. It is not a chronicle of Watergate, nor of the way the two reporters built up the story and gained the support of their editor, Mr Bradlee, and proprietor, Katharine Graham. For that, you would need to read "The Secret Man" alongside "All the President's Men" (1974) and "The Final Days" (1976).

What it is, however, is an exploration of two things: of how and why Mr Felt became an informant; and of the duties owed by journalists to their confidential sources. The first of those Mr Woodward explores in a disarmingly modest but also necessarily incomplete way. His stories of how his own mistakes angered Mr Felt, and put his continuing co-operation at risk, are intriguing, both in themselves and for making one ponder how things might have turned out differently had Deep Throat gone silent. He wasn't the only source that Messrs Woodward and Bernstein had, but he was a crucial one.

Unless Mr Felt turns out to have written a journal or a memoir, we will never know for sure why he provided so much information, for by Mr Woodward's account this nonagenarian has now largely lost his memory. What is clear, however, is that outrage and resentment are not a full explanation. For Mr Felt later authorised his own illegal break-ins, by FBI agents in pursuit of domestic terrorists, for which he was tried, found guilty and subsequently pardoned. His justification, that the country was at war and that the national interest required exceptional measures, might just as well have been Nixon's.

The other question, of journalists' duty to protect their sources, is of current interest thanks to a trial involving reporters from *Time* and the *New York Times*. What "The Secret Man" shows is that, pompous and self-serving though reporters can sound on this issue, the principle is nevertheless vital. Otherwise, Nixon's expletives might never have been deleted.

The Secret Man: The Story of Watergate's Deep Throat.
By Bob Woodward.
Simon & Schuster; 256 pages; $23

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American letters

The light of an oncoming train

Jul 7th 2005
From The Economist print edition

WHEN Robert Lowell died in 1977 at the age of 60, America lost its greatest living poet. Lowell's declamatory and often bruisingly rhetorical verse grew out of a tortured, manic life. It influenced a whole generation of confessional poets, who came to maturity in the 1960s and who included among their number John Berryman and Anne Sexton.

Two years ago, the long-awaited volume of his collected poems was published. Now, with the appearance of his letters, from the same publisher, it is possible for the first time to step behind the often grandiose mask of the poet and compare the work with the circumstantial details of the life.

Lowell was born into a patrician Boston family, but he had a stubborn and independent streak. His early letters to his parents have a ferociously self-righteous directness. Saskia Hamilton, who has edited this collection of letters, likens Lowell to a racehorse in a stall, "tensed for release on to the track of a poem". With the very first letter, written when he was at Harvard in 1936 to a fellow American poet, Ezra Pound, Lowell's prose, though not written and re-written as the poems so often were, releases the same gulping, voracious, exuberant energy as the verse; the same sense that sparks are flying from an anvil as he writes.

The Letters of Robert Lowell
Edited by Saskia Hamilton

Farrar, Straus and Giroux; 849 pages; $40.
Faber and Faber; £30

Buy it at
Amazon.com
Amazon.co.uk

I want to "forge my way into reality," declares the 19-year-old poet to the older man, and that was Lowell's ambition, lifelong. His rise to fame was rapid. By the age of 29, he had published two much praised collections of verse (one of which won the Pulitzer prize), and had been appointed consultant in poetry to the Library of Congress. The letters teem with poetry shoptalk, booklists—Lowell was always striving to be scholarly—news of family feuds, literary acquaintances and politics.

Lowell was always politically engaged. In 1943 he served time in jail for refusing military conscription in protest against the allied bombing of German cities. Two decades on he was campaigning tirelessly against the Vietnam war.

This book faithfully records these literary, political and domestic engagements but, more importantly, it documents the driving passions of a man who, in his own words, was often a wayward and unpredictable mixture of "stiffness and disorder—lethargy and passions". His marriages and many affairs were a painful mess, made all the worse by his mental instability. When he died of a heart attack, in a taxi, he was travelling back to the home of a wife he had divorced, clutching a portrait of the wife to whom he was still notionally married.

What Lowell once wrote about the writing of his poems could just as well serve as a description of the way that he lived his life, headlong from first to last: "We seem to have to go at it with such single-minded intensity that we are always on the point of drowning." These letters are the testament of a man who spent much time just managing not to drown. The marvel is that he was able to describe it all in letters and poems of such force and individuality. "Darkness honestly lived through is a place of wonder and life," he commented, unflinchingly, in 1957.

The Letters of Robert Lowell.
Edited by Saskia Hamilton.
Farrar, Straus and Giroux; 849 pages; $40.
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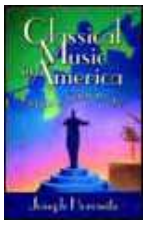
Music

Sinking notes

Jul 7th 2005
From The Economist print edition

Classical Music in America: A History of its Rise and Fall
By Joseph Horowitz



Norton; 606 pages; $39.95

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PERHAPS the most vivid historical writing proceeds from personal engagement. The genesis of Joseph Horowitz's magisterial survey ultimately dates from his realisation, at college, "that there was something incongruous about being at one and the same time an American and a passionate devotee of classical music." Since then, as author and adviser to leading orchestras, he has tried to relate the artistic heritage of the old world to the restless, uncharted territory of the new, and this volume sums up a lifetime's reflections and frustrations.

In a nutshell, the problem is that "America's musical high culture has at all times (alas) been less about music composed by Americans than about American concerts of music composed by Europeans." More's the pity, since in the Gilded Age of the late 19th century America seemed full of possibility, spearheaded by such visionary movers as Henry Higginson, the founder of the Boston Symphony Orchestra. Indeed, Boston prided itself on its connoisseurship and produced a number of talented composers, who sought to adapt the great German tradition to American themes. Music lovers in New York were even more extrovert (and to the Bostonians, unruly) in their passion for Wagner. They too supported the creation of an American school of composers, encouraged by Dvorak, who premiered his "New World Symphony" in the city and praised Negro spirituals as rich material for native composition.

As Mr Horowitz points out, American appreciation of classical music was distinguished by its moral and spiritual intensity—what he terms "sacralisation". In Boston, Beethoven was literally good for the soul; New Yorkers viewed Wagner's Siegfried as the embodiment of American idealism. But after the first world war, that exalted view came to be associated more with the experience of old works than the creation of new ones, and performers inexorably eclipsed composers. Rugged individualists such as Charles Ives were shunned by the classical establishment, as were the likes of George Gershwin, who dared to incorporate jazz.

In a culture increasingly driven by market forces, the new stars were charismatic conductors such as Arturo Toscanini and Leopold Stokowski. But Stokowski's insistence on performing new works diminished his popularity, the same fate that befell Boston's Serge Koussevitzky. Conversely, according to the author, Koussevitzky's hugely promising protégé, Leonard Bernstein, never fulfilled his artistic potential because he was "upstaged by his own celebrity". Even more powerful than the conductors were the soloists: legendary pianists such as Vladimir Horowitz, commanding staggering fees and performing the same repertoire of works on endless tours, basked in the kind of réclame bestowed on film stars. But they offered nothing new or American.

In recent years, as a result of such stultifying repetition, a refusal to engage with the realities of time and place and the irresistible rise of pop culture, the bottom has finally dropped out of the classical music market. Formerly august, unassailable institutions are fighting for survival. Mr Horowitz offers no easy solutions to a crisis that he sees as inherent in the very contradictions of classical music in America. There may be hope in the creative eclecticism of such composers as John Adams and the ambitious, wide-ranging programming of conductors like Michael Tilson Thomas at the San Francisco Symphony Orchestra.

In the meantime, as a comprehensive, convincing analysis of the contemporary dilemma, and a riveting portrait of the century and a half of events and personalities which brought it about, Mr Horowitz's account would be hard to beat.

Classical Music in America: A History of its Rise and Fall.
By Joseph Horowitz.
Norton; 606 pages; $39.95

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New fiction

The law was blind, and Sir Valiant too

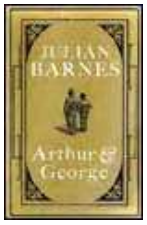
Jul 7th 2005
From The Economist print edition

JULIAN BARNES'S new novel is a departure. Don't expect a dance of ideas or a virtuosic concert of voices. Not that they're exactly missing, but there is less sparkle. Aptly so, perhaps. Of the book's two heroes, the more heroic is the one who loves railway timetables.

"Arthur" is Sir Arthur Conan Doyle, Sherlock Holmes's creator, who was also an ex-ophthalmologist and paid-up spiritualist. "George" is George Edalji, the forgotten "English Dreyfus", victim of a racist miscarriage of justice which shocked Edwardian England. His mother was Scottish, his father a Parsee who converted to Christianity and became vicar of Great Wyrley in darkest Staffordshire. As protection against routine racism, George developed a faith in the rule of law and qualified as a solicitor. He also wrote a book called "Railway Law for the 'Man in the Train' ".

The central irony is that this literal-minded man, for whom truth was something verifiable, like the 07.39 to Birmingham, became the baffled victim of a grotesque fantasy. Police, lawyers, judge and jury, all persuaded themselves, on crazy evidence, that he was behind a series of foul anonymous letters, and a string of midnight horse-slashings. He was sentenced to seven years' hard labour.

Arthur & George
By Julian Barnes



Knopf; 400 pages; $24.95
Jonathan Cape; 360 pages; £17.99.

Buy it at
Amazon.com
Amazon.co.uk

Enter Conan Doyle, a blazing Sir-Valiant-for-Truth, vowing to right this wrong. He too had a truth-distorting story: a fondly loved tubercular wife, and an ecstatically loved second woman. Chivalrous to the first, he assuaged his guilt through abstinence with the second. Either way, honour was compromised. Threads of irony run everywhere. High on indignation, Arthur (to George's embarrassment) accused someone else on evidence as flimsy as the enemy's. The eye-doctor and believer in clairvoyance couldn't see straight. George, shortsighted as well as sceptical, saw more.

These are slightly strained paradoxes, but behind them is something soberingly familiar: "institutional racism", of course, but also the fragility of the law in the face of unblushing authority. The government of the day stonewalled Conan Doyle and thousands of petitioners. It found a "good day to bury" a critical report, to use a current phrase. After three years, the home secretary did release George—but gracelessly, without apology or compensation.

Arthur & George.
By Julian Barnes.
Jonathan Cape; 360 pages; £17.99.
To be published in America by Knopf in January 2006

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Economist.com PRINT EDITION OBITUARY
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Obituary

Jack Kilby

Jul 7th 2005
From The Economist print edition

Corbis

Jack St. Clair Kilby, co-inventor of the integrated circuit, died on June 20th, aged 81

FEW people ever take a look at the innards of their electronic gadgets. But when a mobile phone comes a cropper, all is revealed. Among the shards of glass and bits of metal lie lots of tiny black rectangular chips. These “integrated circuits” are the boxes inside the boxes that make the modern world go.

This wasn't always the case, of course. When Jack Kilby finished his degree in electrical engineering at the University of Illinois in 1947, a computer was something that filled a room and took an army of technicians to maintain. Though the invention of the transistor, by Bell Laboratories in New Jersey, was less than a year away, bulky vacuum tubes still ruled the day. Mr Kilby had deliberately taken extra classes on the physics of vacuum-tube engineering, little knowing that he himself would help to make them obsolete.

In essence, a vacuum tube is a light bulb—an evacuated glass bulb with a metallic filament inside—that can be made into an electrical switch or an amplifier. These were essential components in televisions and radios when Mr Kilby was growing up in Great Bend, Kansas, in the heart of the Great Plains. One day an ice storm blew through the state, bringing down power and telephone lines in its wake. His father, who was in charge of a small electric company, needed to find a way to reach his stranded customers. His solution was amateur radio. Mr Kilby had never before seen the power of electronics to shrink distances and to give people hope. It was, he said later, the moment he decided to make electronics his career.

His first job was with vacuum tubes, at a company called Centralab. There he learned to integrate the tubes into larger circuits, standardising the way they were connected to other components, and helping in the process to make better hearing aids and televisions.

The problems he encountered were shared by all the best engineers of the day. They, like him, could envision countless electrical products that would transform society, but could not make them. Realising their designs would involve assembling and connecting hundreds or thousands of components by hand, using unreliable solder, and then connecting these dinky little constructions to tens of thousands of light bulbs. This “tyranny of numbers” held up technological progress all through the 1950s.

In 1958, Mr Kilby moved his family to Dallas to start work at Texas Instruments. His new job went to the core of the problem: how to make electronic components very, very small. Semiconductor transistors were beginning seriously to rival vacuum tubes. While his colleagues took their holidays, his thoughts began to crystallise into a revolutionary idea.

An electronic circuit is like a symphony played by an orchestra. Depending on how an engineer arranges and connects the capacitors, resistors and transistors, an infinite number of electrical circuits can be created. Engineers had learned that a resistor, which restricts the flow of electrical current, is best made of certain materials and a capacitor, which stores electrical charge, of others.

On July 24th 1958, however (the date was well worth recording), Mr Kilby had a brainwave. Each electronic component, he decided, could be made of the same type of material and integrated into a whole. By carefully controlling its properties, he could turn a single chip of semiconductor into resistors, capacitors and transistors connected in any way he liked.

Smaller and smaller

By September 12th, the idea lay in his hand. It was tiny: a sliver of germanium on a piece of glass, half the size of a paper-clip, with a few wires sticking out to connect it to an oscilloscope. As his colleagues watched, he threw a switch, and the circuit worked. Four months later, Robert Noyce, working in what became known as Silicon Valley, had the same idea. Together, though in amiable rivalry, the two men defeated the tyranny of numbers.

The first integrated circuits, with their mere tens of components, met some scepticism. They did not find commercial favour until 1966, when Mr Kilby used them to make the first hand-held calculator. After that, engineers squeezed more and more components on to ever smaller chips. Today's Pentium 4 chip boasts 169m transistors. The spread of Mr Kilby's invention into never-thought-of applications, and the staggering fall in its cost, never ceased to astonish and delight him.

In 2000, Mr Kilby shared the Nobel prize for physics. (He was sorry that Noyce, who died in 1990, could not share it with him.) Despite the fact that computers and mobile phones relying on integrated circuits were nearly ubiquitous by then, he was still little known, even in Dallas. Like the integrated circuits he had invented, Mr Kilby did not live in the limelight. As long as he had some problem on which to exercise his creativity, and a Big Band radio station to listen to, he was content.

In his Nobel prize lecture, he looked out upon the world that his idea had made possible. In his slow mid-western drawl, he quoted fellow Nobel laureate Charles Townes, the inventor of the laser: “It's like the beaver told the rabbit as they stared at the Hoover Dam. ‘No, I didn't build it myself. But it's based on an idea of mine!’”

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Overview

Jul 7th 2005
From The Economist print edition

Oil, credit and the dollar all became more expensive. The **dollar** strengthened against the euro and the yen: on July 1st the euro bought less than $1.20 for the first time since May 2004. The price of **oil** set a new record: a barrel of West Texas Intermediate, a benchmark crude, fetched more than $61 during trading on July 6th. The Federal Reserve raised **interest rates** by 0.25% to 3.25% on June 30th. However, it gave no hint of a break in its measured pace of monetary tightening.

In **America**, surveys of economic activity found much to cheer. The Institute for Supply Management's manufacturing index rose unexpectedly to 53.8 in June, from 51.4 in May. Its non-manufacturing index leapt from 58.5 to 62.2. A reading above 50 suggests the sector is expanding. **Personal income** rose by 0.2%, or $23.5 billion, in May. Wages and salaries grew by only 0.1%.

Japan's Tankan survey revealed a marked improvement in the mood of large firms in the second quarter. The core consumer-price index (excluding food prices) remained unchanged in the year to May.

In the **euro area**, retail trade grew by 2.0% in the year to May. But GDP in the **Netherlands** shrank by 0.8% in the first quarter, not by 0.1% as originally estimated.

Britain's industrial output fell by 1.9% in the year to May.

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Output, demand and jobs

Jul 7th 2005
From The Economist print edition

% change on year ago

	GDP latest		GDP qtr*	The Economist poll GDP forecasts 2005	2006	Industrial production latest		Retail sales (volume) latest		Unemployment % rate latest		year ago
Australia	+ 1.9	Q1	+ 2.8	+ 2.4	+ 3.1	+ 1.2	Q1	+ 1.8	Q1	5.0	Jun	5.6
Austria	+ 2.0	Q1	+ 0.8	+ 1.9	+ 2.0	+ 3.2	Apr	– 2.4	Apr	4.6	May	4.4
Belgium	+ 1.8	Q1	– 0.1	+ 1.2	+ 1.9	– 1.5	Apr	+ 3.4	Apr	12.2	May†	12.3
Britain	+ 2.1	Q1	+ 1.5	+ 2.2	+ 2.2	– 1.9	May	+ 1.3	May	4.7	Apr††	4.8
Canada	+ 3.3	Q1	+ 2.3	+ 2.8	+ 3.0	+ 1.7	Apr	+ 4.0	Mar	6.8	May	7.1
Denmark	+ 0.8	Q1	+ 0.6	+ 2.1	+ 2.2	– 2.4	Apr	+ 8.7	May	5.9	May	6.5
France	+ 1.8	Q1	+ 1.4	+ 1.5	+ 1.9	nil	Apr	+ 1.5	May	10.2	May	10.0
Germany	+ 1.1	Q1	+ 4.2	+ 1.1	+ 1.3	+ 2.0	Apr	+ 2.7	May	11.7	Jun§	10.5
Italy	– 0.2	Q1	– 1.8	– 0.2	+ 1.1	+ 0.8	Apr	– 4.6	Apr	7.8	Mar	8.2
Japan	+ 1.3	Q1	+ 4.9	+ 1.6	+ 1.8	+ 0.9	May	+ 3.6	Apr	4.4	May	4.6
Netherlands	– 0.5	Q1	– 3.2	+ 0.5	+ 1.5	– 0.7	Apr	– 2.8	Apr	6.6	May**	6.5
Spain	+ 3.3	Q1	+ 3.5	+ 3.1	+ 2.8	+ 0.5	May	+ 2.2	May	9.9	May	11.1
Sweden	+ 1.4	Q1	+ 1.1	+ 1.9	+ 2.6	– 2.1	Apr	+ 4.8	May	5.2	May†	5.7
Switzerland	+ 0.8	Q1	+ 0.2	+ 0.9	+ 1.5	– 0.3	Q1	+ 2.7	Apr	3.6	Jun†	3.7
United States	+ 3.7	Q1	+ 3.8	+ 3.5	+ 3.2	+ 2.7	May	+ 4.3	May	5.1	May	5.6
Euro area	+ 1.3	Q1	+ 2.0	+ 1.3	+ 1.7	+ 0.9	Apr	+ 2.0	May	8.8	May	8.9
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 2.0	Q1	+ 0.5	na	na	– 7.5	May	+ 6.4	Apr	10.2	May†	11.6
Greece	+ 3.5	Q1	na	na	na	– 3.2	Apr	+ 3.5	Apr	10.2	Dec	9.8
Iceland	+ 2.9	Q1	na	na	na	na		na		2.3	Apr†	3.5
Ireland	+ 2.8	Q4	na	na	na	– 6.4	Apr	+ 3.9	Apr	4.2	Jun	4.4
Luxembourg	+ 3.8	Q4	na	na	na	+ 2.4	Mar	– 3.5	May	4.5	May	3.9
New Zealand	+ 1.9	Q1	+ 1.5	na	na	+ 3.5	Q4	+ 5.8	Q1	3.9	Q1	4.2
Norway	– 0.8	Q1	+ 2.2	na	na	+ 4.0	Apr	+ 7.2	May	4.6	May**	4.3
Portugal	+ 0.1	Q1	+ 0.8	na	na	– 4.7	May	+ 2.5	May	7.5	Q1†	6.4

*% change on previous quarter at an annual rate. †Not seasonally adjusted. ‡New series. ††Feb-Apr; claimant count rate 2.7% in May. §EU harmonised rate 9.3% in May. **Mar-May.

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Prices and wages

Jul 7th 2005
From The Economist print edition

% change on year ago

	Consumer prices			The Economist poll consumer prices forecast		Producer prices			Wages/earnings		
	latest		year ago	2005	2006	latest		year ago	latest		year ago
Australia	+ 2.4	Q1	+ 2.0	+ 2.7	+ 2.6	+ 6.0	Q1	– 1.1	+ 4.5	Q1	+ 5.0
Austria	+ 2.3	May	+ 2.1	+ 2.1	+ 1.7	+ 0.7	Jun	+ 5.9	+ 2.3	May	+ 2.1
Belgium	+ 2.9	Jun	+ 2.3	+ 2.1	+ 1.7	+ 2.4	May	+ 3.9	+ 2.6	Apr	+ 2.3
Britain	+ 1.9	May*	+ 1.5	+ 1.9	+ 1.9	+ 2.7	May	+ 2.5	+ 4.6	Apr†	+ 4.4
Canada	+ 1.6	May	+ 2.5	+ 2.1	+ 2.2	– 0.3	May	+ 6.4	+ 3.1	Apr	+ 3.3
Denmark	+ 1.5	May	+ 1.3	+ 1.4	+ 1.7	+ 3.0	May	+ 2.8	+ 3.1	Q1	+ 3.3
France	+ 1.5	May	+ 2.6	+ 1.7	+ 1.6	+ 2.4	May	+ 2.2	+ 2.9	Q1	+ 2.8
Germany	+ 1.9	Jun	+ 1.7	+ 1.4	+ 1.1	+ 1.7	May	+ 3.6	+ 1.6	Apr	+ 1.1
Italy	+ 1.8	Jun	+ 2.4	+ 2.0	+ 1.9	+ 3.1	May	+ 2.9	+ 3.1	May	+ 3.3
Japan	+ 0.2	May	– 0.5	– 0.1	+ 0.2	+ 1.8	May	+ 0.9	– 0.2	May	+ 2.2
Netherlands	+ 1.6	Jun	+ 1.4	+ 1.4	na	+ 3.3	May	+ 4.2	+ 0.6	May	+ 1.5
Spain	+ 3.1	May	+ 3.4	+ 3.0	+ 2.7	+ 4.2	May	+ 3.8	+ 3.0	Q1	+ 3.2
Sweden	+ 0.1	May	+ 0.7	+ 0.5	+ 1.4	+ 2.4	May	+ 1.2	+ 1.3	Apr	+ 2.9
Switzerland	+ 0.7	Jun	+ 1.1	+ 1.1	+ 1.1	+ 0.5	May	+ 1.4	+ 0.9	2004	+ 1.4
United States	+ 2.8	May	+ 3.1	+ 2.9	+ 2.5	+ 3.5	May	+ 4.7	+ 2.6	May	+ 2.0
Euro area	+ 2.1	Jun	+ 2.4	+ 1.9	+ 1.5	+ 3.5	May	+ 2.4	+ 3.1	Q1	+ 3.0
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 0.8	May	– 0.1	na	na	+ 2.3	May	+ 1.7	+ 4.1	Q1	+ 4.2
Greece	+ 3.2	May	+ 2.9	na	na	+ 3.0	May	+ 6.0	na		na
Iceland	+ 2.8	Jun	+ 3.9	na	na	+ 4.2	Jun	+ 5.3	+ 6.6	May	+ 4.6
Ireland	+ 2.4	May	+ 1.7	na	na	– 2.2	May	– 0.1	+ 5.1	Q4	+ 4.5
Luxembourg	+ 2.4	May	+ 2.3	na	na	+ 8.9	Apr	+ 6.2	+ 1.8	Mar	+ 2.1
New Zealand	+ 2.8	Q1	+ 1.5	na	na	+ 4.2	Q1	– 0.6	+ 2.5	Q1	+ 2.2
Norway	+ 1.6	May	+ 1.0	na	na	+ 9.2	May	+18.8	+ 3.7	Q1	+ 3.5
Portugal	+ 1.8	May	+ 2.4	na	na	+ 3.9	May	+ 1.9	– 1.6	Apr	– 1.4

*New series. RPI inflation rate 2.9% in May. †Feb-Apr.

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Economic forecasts

Jul 7th 2005
From The Economist print edition

The Economist poll of forecasters, July averages (previous month's, if changed)

	Real GDP, % change Low/high range		Real GDP, % change average		Consumer prices % increase		Current account % of GDP	
	2005	2006	2005	2006	2005	2006	2005	2006
Australia	2.0/3.4	2.7/3.6	2.4 (2.6)	3.1 (3.2)	2.7 (2.6)	2.6	-5.8(-5.7)	-5.5 (-5.1)
Austria	1.6/2.3	1.5/2.2	1.9 (2.0)	2.0	2.1	1.7 (1.6)	-0.4(-0.5)	-0.4 (-0.6)
Belgium	0.9/1.5	1.5/2.3	1.2 (1.6)	1.9 (2.1)	2.1 (2.0)	1.7	3.0 (3.3)	3.0 (3.3)
Britain	1.8/2.8	1.7/2.6	2.2 (2.4)	2.2 (2.1)	1.9	1.9	-2.4(-2.5)	-2.5
Canada	2.3/3.1	2.5/3.7	2.8 (2.6)	3.0 (2.9)	2.1	2.2 (2.1)	1.3 (1.7)	1.1 (1.5)
Denmark	1.5/2.4	1.8/2.5	2.1	2.2	1.4	1.7	2.0 (2.1)	1.9 (2.1)
France	1.3/1.9	1.6/2.2	1.5 (1.8)	1.9 (2.0)	1.7 (1.6)	1.6	-0.6(-0.3)	-0.3 (-0.1)
Germany	0.9/1.4	1.0/1.6	1.1	1.3 (1.4)	1.4	1.1 (1.0)	3.5 (3.4)	3.3 (3.2)
Italy	-0.6/0.7	0.6/1.6	-0.2 (0.3)	1.1 (1.3)	2.0 (1.9)	1.9 (1.8)	-1.2	-1.3 (-1.2)
Japan	1.2/2.0	1.0/2.9	1.6 (1.4)	1.8	-0.1	0.2 (0.3)	3.6	3.5 (3.6)
Netherlands	0.1/1.2	0.8/2.2	0.5 (0.8)	1.5 (1.6)	1.4	na	3.7 (3.4)	3.6 (3.4)
Spain	2.5/3.3	2.3/3.2	3.1 (2.8)	2.8 (2.7)	3.0 (2.9)	2.7	-5.2(-4.9)	-5.3 (-4.9)
Sweden	0.4/2.7	1.8/2.9	1.9 (2.8)	2.6 (2.8)	0.5 (0.7)	1.4 (1.5)	7.0 (6.9)	6.4 (6.3)
Switzerland	0.3/1.2	0.7/2.0	0.9 (1.2)	1.5 (1.7)	1.1 (1.2)	1.1 (1.2)	11.4(11.1)	10.8 (10.6)
United States	3.2/3.7	2.2/4.1	3.5	3.2	2.9	2.5	-6.3	-6.2
Euro area	1.1/1.4	1.3/2.0	1.3 (1.4)	1.7 (1.8)	1.9 (1.8)	1.5	0.5	0.4 (0.5)

Sources: ABN Amro, Deutsche Bank, Economist Intelligence Unit, Goldman Sachs, HSBC Securities, KBC Bank, J.P. Morgan Chase, Morgan Stanley, Decision Economics, BNP Paribas, Royal Bank of Canada, Citigroup, Scotiabank, UBS

Every month, *The Economist* surveys a group of forecasters and calculates the average of their predictions for economic growth, inflation and current-account balances for 15 countries and for the euro area. The table also shows the highest and lowest projections for growth. The previous month's figures, where they are different, are shown in brackets. The panel has cut its growth forecast for the euro area to 1.3% in 2005 and 1.7% in 2006, down from 1.4% and 1.8% respectively last month. It now expects GDP in Italy to contract by 0.2% this year whereas it predicted growth of 0.3% in June. France is forecast to grow by 1.5% in 2005, compared with 1.8% last month. The panel has also become gloomier about British growth in 2005, which it has cut from 2.4% to 2.2%. However, it has raised its forecast for Japanese growth in 2005 to 1.6%, up from 1.4% in June.

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Money and interest rates

Jul 7th 2005
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	Money supply* % change on year ago			Interest rates % a year (Jul 6th 2005)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+ 5.4	+ 9.2	May	5.65	5.48	5.14	5.13	5.80	6.20
Britain	+ 4.3	+11.6	May	4.64	4.78	4.14	4.28	5.02	5.20
Canada	+10.3	+ 9.8	May	2.52	2.00	2.97	3.95	4.82	5.20
Denmark	+16.2	+ 9.0	May	2.20	2.25	2.12	3.16	4.34	4.92
Japan	+ 4.0	+ 1.5	May	0.02	0.02	0.08	1.24	1.77	1.32
Sweden	+ 2.5	+ 4.7	May	1.49	1.98	1.86	3.02	4.51	2.70
Switzerland	- 7.3	+ 2.3	May	0.75	0.48	0.83	1.94	2.84	1.89
United States	+ 2.7	+ 4.3	May	3.51	1.49	3.76	4.07	4.47	5.05
Euro area†	+10.1	+ 7.3	May	2.12	2.11	2.13	3.19	4.19	3.43

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. † Germany for bonds. Benchmarks: US 30-year 4.33%, Japan No. 271 1.25%. Central bank rates: US fed funds 3.25%, ECB refinancing 2.00%, BOJ overnight call 0.001%, BOE repo 4.75%. Sources: Bank of Canada, Commerzbank, Danske Bank, J.P. Morgan Chase, Stockholmsbörsen, UBS, Global Insight, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Jul 7th 2005
From The Economist print edition

2000=100

	Jun 28th	Jul 5th*	% change on one month	% change on one year
Dollar index				
All items	133.4	134.1	– 0.9	– 0.3
Food	128.8	131.0	+ 0.4	– 3.7
Industrials				
All	139.4	138.1	– 2.6	+ 4.1
Nfa†	131.9	135.3	+ 4.0	+ 0.4
Metals	143.5	139.6	– 5.8	+ 6.2
Sterling index				
All items	111.3	115.9	+ 3.3	+ 4.5
Euro index				
All items	102.1	104.1	+ 2.1	+ 2.7
Yen index				
All items	135.9	139.0	+ 3.7	+ 1.9
Gold				
$ per oz	436.45	423.15	– 0.5	+ 8.2
West Texas Intermediate				
$ per barrel	58.25	59.57	+10.8	+50.2

* Provisional. † Non-food agriculturals.

Our commodity-price index was rebased in February 2005

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Stockmarkets

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Market indices

	Jul 6th	2005 high	2005 low	% change on one week	% change on record high	% change on Dec 31st 2004 in local currency	% change on Dec 31st 2004 in $ terms
Australia (All Ordinaries)	4,234.1	4,267.3	3,905.5	+ 0.4	- 0.8	+ 4.5	- 1.0
Austria (ATX)	3,084.2	3,099.5	2,415.0	+ 1.9	- 0.5	+26.9	+11.3
Belgium (Bel 20)	3,121.9	3,197.3	2,958.8	+ 0.3	-15.2	+ 6.5	- 6.6
Britain (FTSE 100)	5,229.6	5,229.6	4,783.6	+ 2.4	-24.5	+ 8.6	- 0.5
Canada (Toronto Composite)	10,111.9	10,111.9	9,006.2	+ 0.8	-11.2	+ 9.4	+ 6.0
Denmark (KBX)	314.1	314.1	257.8	+ 1.1	nil	+21.8	+ 6.7
France (SBF 250)	2,975.6	2,975.6	2,633.6	+ 1.3	-32.2	+13.0	- 0.9
(CAC 40)	4,280.0	4,280.0	3,816.1	+ 1.1	-38.2	+12.0	- 1.7
Germany (DAX)*	4,615.5	4,627.5	4,178.1	+ 0.7	-42.8	+ 8.4	- 4.8
Italy (S&P/MIB)	32,731.0	32,856.0	30,645.0	+ 1.7	-34.7	+ 5.9	- 7.1
Japan (Nikkei 225)	11,603.5	11,966.7	10,825.4	+ 0.2	-70.2	+ 1.0	- 7.4
(Topix)	1,183.6	1,203.3	1,109.2	+ 0.6	-59.0	+ 3.0	- 5.6
Netherlands (AEX)	390.3	390.3	347.0	+ 1.8	-44.4	+12.1	- 1.6
Spain (Madrid SE)	1,062.1	1,062.1	950.9	+ 0.8	- 7.3	+10.7	- 2.8
Sweden (Affarsvarlden Gen)	250.8	250.8	218.9	+ 1.5	-37.3	+13.4	- 4.3
Switzerland (Swiss Market)	6,309.0	6,309.0	5,669.6	+ 0.8	-25.0	+10.8	- 3.3
United States (DJIA)	10,270.7	10,940.6	10,012.4	- 1.0	-12.4	- 4.8	- 4.8
(S&P 500)	1,194.9	1,225.3	1,137.5	- 0.4	-21.8	- 1.4	- 1.4
(NASDAQ Comp)	2,068.7	2,152.2	1,904.2	nil	-59.0	- 4.9	- 4.9
Europe (FTSEurofirst 300)†	1,157.2	1,157.2	1,038.6	+ 1.2	-32.1	+11.1	- 2.5
Euro area (FTSE Euro 100)†	980.6	980.6	894.4	+ 1.3	-36.8	+ 8.8	- 4.5
World (MSCI)‡	1,150.0	1,193.0	1,115.0	- 0.3	-20.6	- 1.7	- 1.7
World bond market (Citigroup)††	630.0	662.3	629.6	- 1.4	- 4.9	- 5.4	- 5.4

*Total return index. †In euro terms. ‡Morgan Stanley Capital International index includes individual markets listed above plus eight others, in $ terms. ††Citigroup World Government Bond Index, total return, in $ terms.

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Trade, exchange rates and budgets

Jul 7th 2005
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	Trade balance*, $bn latest 12 months		Current-account balance $bn latest 12 mths		The Economist poll % of GDP, forecast 2005	2006	Exchange rate trade-weighted† 2000=100 Jul 6th	year ago	Currency units per $ Jul 6th	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2005‡
Australia	− 18.1	May	− 42.4	Q1	− 5.8	− 5.5	116.2	110.7	1.35	1.38	2.37	1.61	1.20	+ 0.9
Austria	+ 0.1	Apr	+ 0.6	Apr	− 0.4	− 0.4	104.8§	103.6	0.84	0.81	1.47	–	0.75	− 2.0
Belgium	+ 16.7	Mar	+ 8.6	Apr	+ 3.0	+ 3.0	105.5§	103.9	0.84	0.81	1.47	–	0.75	− 0.5
Britain	−109.9	Apr	− 44.0	Q1	− 2.4	− 2.5	99.1	102.3	0.57	0.54	–	0.68	0.51	− 2.9
Canada	+ 49.1	Apr	+ 20.2	Q1	+ 1.3	+ 1.1	117.3	108.8	1.24	1.32	2.17	1.47	1.11	+ 1.2
Denmark	+ 9.2	Apr	+ 8.6	Apr	+ 2.0	+ 1.9	105.7	106.0	6.25	6.01	11.0	7.45	5.59	+ 1.8
France	− 22.4	Apr	− 19.4	Apr	− 0.6	− 0.3	108.3§	106.4	0.84	0.81	1.47	–	0.75	− 3.0
Germany	+198.5	Apr	+108.0	Apr	+ 3.5	+ 3.3	106.2§	104.0	0.84	0.81	1.47	–	0.75	− 3.5
Italy	− 6.1	Apr	− 19.0	Apr	− 1.2	− 1.3	77.5§	76.2	0.84	0.81	1.47	–	0.75	− 4.4
Japan	+125.3	Apr	+170.9	Apr	+ 3.6	+ 3.5	86.4	87.8	112	108	197	133	–	− 6.1
Netherlands	+ 38.7	Apr	+ 33.9	Q1	+ 3.7	+ 3.6	105.0§	103.2	0.84	0.81	1.47	–	0.75	− 2.2
Spain	− 85.7	Apr	− 65.8	Mar	− 5.2	− 5.3	77.8§	76.9	0.84	0.81	1.47	–	0.75	+ 0.5
Sweden	+ 22.8	May	+ 29.7	Q1	+ 7.0	+ 6.4	95.2	98.1	7.87	7.42	13.8	9.39	7.04	+ 0.8
Switzerland	+ 6.6	May	+ 40.8	Q4	+11.4	+10.8	106.0	108.7	1.30	1.23	2.29	1.55	1.17	− 1.0
United States	−709.7	Apr	−717.0	Q1	− 6.3	− 6.2	87.1	86.2	–	–	1.76	1.19	0.89	− 4.1
Euro area	+ 69.0	Apr	+ 27.9	Apr	+ 0.5	+ 0.4	114.8	115.2	0.84	0.81	1.47	–	0.75	− 2.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 12.6	Apr	+ 11.8	Apr	na	na	82.4§	81.0	0.84	0.81	1.47	–	0.75	+ 1.3
Greece	− 33.0	Mar	− 11.6	Apr	na	na	60.4§	59.6	0.84	0.81	1.47	–	0.75	− 3.8
Iceland	− 0.8	May	− 1.4	Q1	na	na	105.7**	98.7	65.8	71.6	116	78.5	58.9	+ 1.1
Ireland	+ 40.6	Apr	− 3.1	Q1	na	na	95.9§	93.2	0.84	0.81	1.47	–	0.75	− 0.7
Luxembourg	− 4.3	Apr	+ 2.9	Q4	na	na	105.5§	103.9	0.84	0.81	1.47	–	0.75	− 0.8
New Zealand	− 3.4	May	− 7.0	Q1	na	na	134.2	128.2	1.49	1.52	2.62	1.78	1.33	+ 3.2
Norway	+ 41.9	May	+ 37.9	Q1	na	na	110.0	103.0	6.64	6.82	11.7	7.92	5.94	+ 14.4
Portugal	− 19.6	Mar	− 14.4	Apr	na	na	94.3**	94.0	0.84	0.81	1.47	–	0.75	− 5.3

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, April average. ‡OECD forecast. **IMF, February average.

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Commercial property prices

Jul 7th 2005
From The Economist print edition

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Overview

Jul 7th 2005
From The Economist print edition

Thanks to higher oil prices, **Russia's** current-account surplus widened to $69.3 billion in the year to March, almost twice as large as a year ago. Russia now has the biggest surplus of the emerging economies in our table.

Argentina's inflation rate jumped to 9.0% in the 12 months to June, up from 4.9% a year earlier. **Thailand's** inflation rate also rose in June, to 3.8%, it highest for six years.

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Cost of living index

Jul 7th 2005
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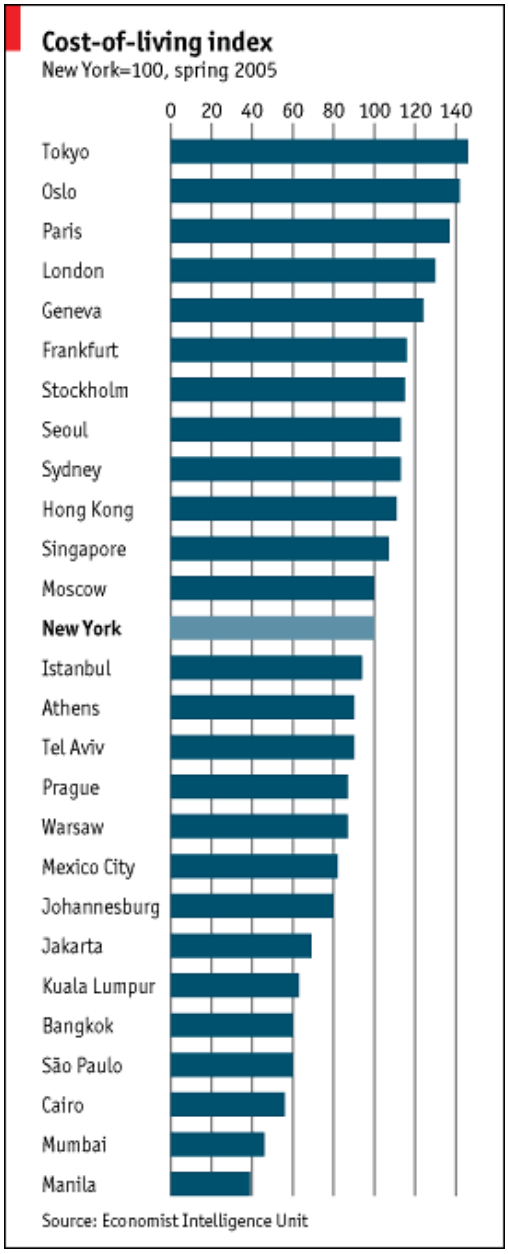
Tokyo is still the most expensive city in the world for expatriates, according to a survey of 127 cities by The Economist Intelligence Unit, a sister company of *The Economist*. Close behind are Oslo, Paris and London. By contrast, New York looks a bargain: average living costs are 32% cheaper than in Tokyo and 23% less than in London. At the other extreme, living in Manila or Mumbai costs less than half as much as in New York.



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Economy

Jul 7th 2005
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	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 9.4	Q1	+16.6	May	+ 1.8	May	+71.1	May	+68.7	2004	659.1	Mar
Hong Kong	+ 6.0	Q1	– 0.6	Q1	+ 0.8	May	–10.3	May	+18.5	Q1	122.4	May
India	+ 7.0	Q1	+ 8.8	Apr	+ 3.7	May	–30.6	May	– 6.4	Q1	134.0	May
Indonesia	+ 6.4	Q1	+10.1	Mar	+ 7.4	Jun	+27.6	May	+ 2.9	Q4	33.3	May
Malaysia	+ 5.7	Q1	– 0.4	May	+ 3.1	May	+23.2	May	+16.7	Q1	74.1	May
Philippines	+ 4.6	Q1	+ 2.5	Apr	+ 7.6	Jun	nil	Mar	+ 2.9	Mar	15.1	Jun
Singapore	+ 2.5	Q1	+ 1.7	May	nil	May	+16.6	May	+29.2	Q1	116.0	May
South Korea	+ 2.7	Q1	+ 4.3	May	+ 2.7	Jun	+27.0	Jun	+23.0	May	206.0	May
Taiwan	+ 2.5	Q1	– 1.4	May	+ 2.4	Jun	+ 2.6	May	+16.9	Q1	253.6	Jun
Thailand	+ 3.3	Q1	+ 8.0	May	+ 3.8	Jun	– 4.4	May	+ 0.1	May	47.1	May
Argentina	+ 8.0	Q1	+ 6.3	May	+ 9.0	Jun	+11.2	May	+ 2.8	Q1	20.1	Apr
Brazil	+ 2.9	Q1	+ 6.3	Apr	+ 8.1	May	+38.3	Jun	+13.4	May	60.7	May
Chile	+ 5.7	Q1	+ 6.8	May	+ 2.7	Jun	+ 8.6	May	+ 1.1	Q1	17.3	May
Colombia	+ 3.6	Q1	+ 4.5	Apr	+ 4.8	Jun	+ 0.8	Jan	– 0.8	Q1	12.2	May
Mexico	+ 2.4	Q1	+ 5.2	Apr	+ 4.6	May	– 9.9	May	– 8.7	Q1	62.8	Apr
Peru	+ 6.4	Apr	+ 7.1	Apr	+ 1.5	Jun	+ 3.3	Apr	+ 0.4	Q1	12.8	Apr
Venezuela	+ 7.9	Q1	+28.2	Apr	+15.9	Jun	+22.6	Q1	+14.9	Q1	19.9	Mar
Egypt	+ 4.7	Q4	+ 3.3	2004†	+ 4.7	Apr	– 9.0	Q4	+ 4.3	Q4	16.8	Apr
Israel	+ 4.1	Q1	+12.8	Apr	+ 0.2	May	– 7.2	May	+ 1.9	Q1	26.5	Jun
South Africa	+ 4.2	Q1	+ 7.1	Apr	+ 3.3	May	– 2.7	May	– 8.5	Q1	16.9	Jun
Czech Republic	+ 4.4	Q1	+ 5.7	Apr	+ 1.3	May	+ 0.7	May	– 4.4	Q1	27.1	May
Hungary	+ 2.9	Q1	+10.1	May	+ 3.6	May	– 2.7	Q1	– 9.2	Q1	17.5	May
Poland	+ 2.1	Q1	+ 0.9	May	+ 2.5	May	– 3.7	Apr	– 1.1	Apr	39.3	Apr
Russia	+ 5.2	Q1	+ 1.4	May	+13.5	May	+101.0	Apr	+69.3	Q1	143.6	May
Turkey	+ 4.8	Q1	+ 5.1	Apr	+ 9.0	Jun	–36.3	Apr	–17.2	Apr	35.8	May
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Estonia	+ 7.2	Q1	+ 8.4	May	+ 2.8	May	– 2.4	Apr	– 1.3	Apr	1.7	Apr
Latvia	+ 7.4	Q1	+ 4.3	Apr	+ 6.3	May	– 3.0	Apr	– 1.6	Apr	2.0	Apr
Lithuania	+ 5.6	Q1	na		+ 2.0	May	– 3.0	Apr	– 1.6	Q4	3.6	Apr
Slovakia	+ 5.1	Q1	+ 5.1	Apr	+ 2.4	May	– 1.9	Apr	– 1.8	Mar	17.6	Apr
Slovenia	+ 2.6	Q1	+ 3.7	Apr	+ 2.2	May	– 1.4	Apr	– 0.2	Apr	8.4	Mar
Pakistan	+ 6.4	2004†	+ 9.6	Jan	+ 9.8	May	– 6.2	May	– 1.5	Q1	10.7	Apr
Saudi Arabia	+ 5.2	2004	na		+ 0.6	Mar	+84.9	2004	+51.5	2004	22.9	Apr

*Excluding gold, except Singapore; IMF definition. †Year ending June.
Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Akbank; Deutsche Bank

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Financial markets

Jul 7th 2005
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Jul 6th		Dec 31st 2004	
	Jul 6th	year ago	Jul 6th	% a year		one week	in local currency	in $ terms
China	8.28	8.28	14.5	4.57	1,085.4	-6.5	- 18.4	- 18.4
Hong Kong	7.77	7.80	13.7	3.53	14,149.9	-0.9	- 0.6	- 0.6
India	43.6	45.8	76.6	5.35	7,287.6	+2.4	+ 10.4	+ 10.1
Indonesia	9,783	9,000	17,197	8.60	1,117.8	-0.8	+ 11.8	+ 6.0
Malaysia	3.80	3.80	6.68	2.88	902.7	+1.4	- 0.5	- 0.5
Philippines	56.1	55.9	98.7	6.81	1,813.0	-6.8	- 0.5	- 0.5
Singapore	1.70	1.71	2.98	2.06	2,234.1	+1.4	+ 8.1	+ 4.1
South Korea	1,049	1,152	1,843	3.53	1,019.0	+2.0	+ 13.7	+ 12.3
Taiwan	31.9	33.5	56.1	1.45	6,222.1	-0.2	+ 1.3	+ 0.6
Thailand	41.6	40.8	73.1	2.75	659.9	-3.7	- 1.2	- 7.7
Argentina	2.88	2.95	5.07	6.81	1,356.2	-1.3	- 1.4	+ 1.6
Brazil	2.39	3.03	4.20	19.72	24,510.2	-2.5	- 6.4	+ 4.1
Chile	584	631	1,026	3.72	9,461.2	-1.1	+ 5.6	+ 0.5
Colombia	2,345	2,681	4,122	7.18	5,570.5	+1.4	+ 28.2	+ 28.6
Mexico	10.8	11.5	18.9	9.61	13,790.2	+1.8	+ 6.8	+ 10.5
Peru	3.25	3.46	5.72	3.03	4,061.4	+0.5	+ 9.5	+ 10.4
Venezuela	2,613§	2,558§	4,593	12.19	21,913.2	+1.5	- 26.8	- 27.8
Egypt	5.78	6.20	10.17	7.90	43,216.7	+3.3	+ 75.8	+ 84.5
Israel	4.60	4.48	8.08	3.65	656.9	-0.4	+ 2.0	- 4.2
South Africa	6.83	6.11	12.0	7.05	14,394.6	+1.5	+ 13.7	- 6.2
Czech Republic	25.2	25.4	44.4	1.75	1,220.8	+1.1	+ 18.3	+ 4.7
Hungary	207	202	365	6.73	19,593.9	+5.2	+ 32.9	+ 15.8
Poland	3.41	3.66	5.99	4.74	28,908.9	+2.9	+ 8.5	- 4.7
Russia	28.8	29.1	50.7	13.00	740.3‡	+6.0	+ 25.4	+ 20.5
Turkey	1.35	1.44	2.37	16.54	27,781.4	+2.4	+ 11.3	+ 11.3
EM (MSCI)*	1.00	1.00	1.76	na	565.5	nil	+ 4.3	+ 4.3
EMBI+†	1.00	1.00	1.76	na	345.5	-0.3	+ 4.8	+ 4.8

*Emerging Mkts. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In $ terms. §Floating exchange rate.
Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Akbank; Deutsche Bank

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